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SPECIAL FINANCIAL ISSUE

FINANCIAL $URVIVAL IN A TROUBLED WORLD

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Who speaks for capitalism in American politics?

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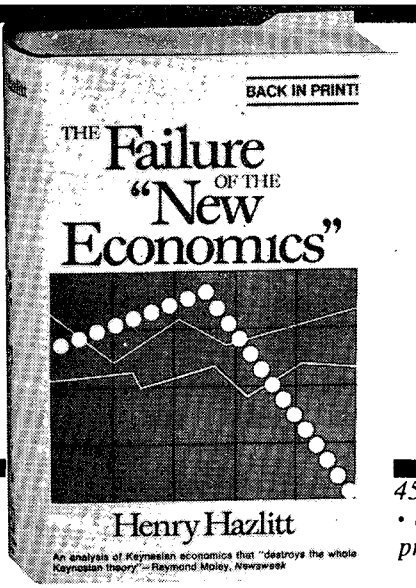
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THE Failure OF THE "New Economics"
Henry Hazlitt
An analysis of Keynesian economics that "destroys the whole Keynesian theory"—Raymond Moley, Newsweek

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458 pages • 4 appendices • 8-page subject and proper-name index

When President Nixon proclaimed himself a Keynesian in the middle of his first term, his words struck some like a thunderclap. A *Republican* President embracing Lord Keynes? Surely the last rampart had fallen . . .

Three years and several Phases later, these observers weren't so sure. Inflation was raging. The dollar was sharply down. Recession—or full-blown depression—loomed. Lord Keynes, it appeared, was really dead.

Earlier, Keynes had been hailed as the peer of Adam Smith, Ricardo, even Darwin. His 1936 book, *The General Theory of Employment, Interest, and Money,* is easily the most influential economic work of the century—the fountainhead of a whole school of thought commonly dubbed the New Economics.

But if President Nixon and his advisors had learned the lessons of this book in 1971, our economy would be healthier today. For in these learned yet lively pages, Henry Hazlitt leaves Keynes prostrate. Chapter by chapter, theorem by theorem, Mr. Hazlitt subjects Keynes to the most searching analysis he has ever undergone.

The great economist challenges every major Keynesian tenet: the attempted refutation of Say's Law; his bias against thrift; the alleged dependence of employment on "the propensity to consume"; his scorn for the gold standard; the "liquidity preference" explanation of interest rates; his attack on "speculation"; above all, the Keynesian view that unemployment is not caused by bloated wages.

Keynes provided the building blocks for much of Nixonomics. Mr. Hazlitt shatters them all:

- deficit financing
- huge public spending
- perpetually low interest rates
- the "national income" approach
- full employment
- paper money
- "acceptable" inflation

Henry Hazlitt concludes:

- ✔ Keynesianism has failed as a tool of economic analysis
- ✔ Keynesianism has failed as a basis of economic forecasting
- ✔ Above all, Keynesianism has failed as a guide to national policy

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special financial issue

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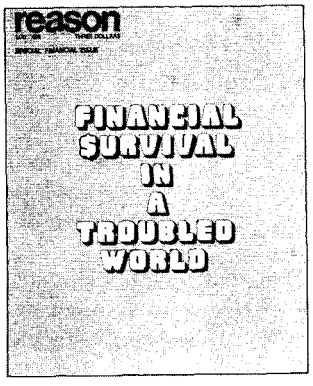

editorial introduction

The Chinese word for "crisis" contains two characters. One of them means opportunity.

The theme of individual economic survival, chosen for this special issue of *REASON* magazine, accurately reflects the challenge we all face today. In turn, the heading to my editorial strongly implies that what we really have is a crisis, but more importantly, a crisis that can be turned to the reader's advantage. But to do so the reader will have to invest his time to carefully re-think many currently accepted investment nostrums. If you want to make this commitment, this issue is the ideal place for you to begin for it constitutes one of the largest, if not the largest, collection of practical financial articles ever assembled for any issue of any magazine. In reality, the issue is a handbook of financial information, but, unlike a book, much of the material has immediate application to the markets of May, 1974.

Looking to the issue itself, you will find articles of several different types. For example, "The Coming Credit Collapse" and "What You Should Know About Monetary and Fiscal Policy" are included because they will provide you a "feel" for the macro-economic environment in which you are living today and bring to your decision-making a general, and I hope, critical understanding of the forces that are now active in the economy. Without such an understanding, valuable investment advice can easily lose meaning when you try to relate it to a nonexistent or shaky frame of reference. In the same vein, articles such as "The Dow Theory Revisited" will help you develop an understanding of the origin and nature of financial analysis, as part of a thorough understanding of financial history, the ideal ally for helping to put new economic developments in proper perspective. You will also find articles critically examining some of the common areas of investment today, notably the stock market and that sacred cow—real estate.

Whether you are a sophisticate or only a recent initiate to the world of investments, the articles on foreign currency trading, cyclicality in stock and commodity prices, and gemstones should be of interest to you as well.

Our emphasis on gold may seem excessive but such is not the case: gold has served for thousands of years as the ideal store of value investment. Unfortunately political developments have prevented American investors from making maximal use of its potentials for several generations. However this is changing rapidly as powerful market forces bring gold back to the forefront once again. Therefore I strongly urge you to place our two interviews near the top of your reading list since they examine in detail all major areas of gold investment used today.

You have an added benefit in the large quantity of specialized advertising in this issue. Advertising, a much maligned and misunderstood institution, should really be appreciated for what it is, a valuable source of consumer information. This issue has over 40 pages of it and the prudent will treat it as their working bibliography for financial success.

With our troubled world and the growing crisis of the economy, it seems only logical that we should look for a reason. That leads directly to the government and its interventionist economic policies, ranging from the flood of vote-buying paper dollars its presses produce to the shortages created when the market's allocative mechanism of price is choked by the heavy hand of governmental control. The government presents two important challenges. First is your personal survival in a politically distorted economy, and second, the necessity of removing the government from those areas that are the appropriate domain of the free market. The growth of government into our personal lives has been a gradual one; the removal will be also. It is a battle that can be won but it will take your personal and ongoing commitment to the libertarian ideal.

If you are new to *REASON* and have not subscribed I invite you to do so now. It is a young and growing magazine of the highest order: its perceptive economic and social analyses will reward careful and thoughtful attention many times over in the ensuing months.

I would like to give special thanks to the staff of *REASON* magazine for their invaluable help and ready cooperation with me in the assemblage of this issue, most notably Robert Poole Jr., and Ms. Lynn Kinsky. Also my sincere appreciation to the authors and advertisers in this issue whose importance is more than obvious.

From myself and the staff of *REASON* comes the profound hope that our readers may survive and prosper.

Robert H. Meier
Special Editor

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GOLD: Yesterday, Today & Tomorrow

Eugene Guccione

In ages past, a government would seize gold and try to palm off bronze or copper coins to its citizens. The modern method has consisted of palming off paper after seizing gold. So there's nothing new in today's governmental attitudes toward gold or other forms of wealth.

Indeed, the one conclusion that can be safely drawn after 30 centuries of fiscal and monetary history is that wealth can be obtained by earning it (which is difficult), or by seizing it—which is much easier, and which is the favorite method of governments.

Of course, if a person seizes another person's property, the action is called a crime; but if done by a government, it is called taxation or "nationalization" or some such euphemism for theft and fraud.

Eugene Guccione, a chemical engineer, is currently president of Mountain States Lime Inc., and R&D vice president of the parent company, Mountain States Resources Corp. (Salt Lake City), which he joined early this year after 14 years in New York as associate editor of McGraw-Hill's CHEMICAL ENGINEERING *and senior editor of* ENGINEERING & MINING JOURNAL. *He is also monetary consultant to Coin America Inc., Phoenix, AZ, and a director of the Committee for Monetary Research & Education, a nonprofit organization in Greenwich, CT.*

It is worth noting that, at least since the Renaissance, the frauds and thefts of monetary history have been interwoven with a new element: lunacy. The alchemists of the Middle Ages, for instance, searched in vain for the philosophers' stone that would change lead into gold. The alchemists of today (often known as "new economists") haven't found the philosophers' stone either—but they have found a substitute: the Keynesian stone. It turns gold into paper. Which is not *too* bad. Paper, after all, is a worthwhile commodity.

Unfortunately, the Keynesian stone has a side effect: it also changes those who touch it into philosopher-kings. Philosopher-kings invariably get into government. And today's government, as Ludwig von Mises has noted, is the only institution that can take a worthwhile commodity like paper, slap some ink on it, and make it totally worthless.

Case in point: the U.S. dollar.

The U.S. dollar is worth 1/42.5 of an ounce of gold, according to current mythology. Like all myths, this too is based on some fragment of fact—which in this case is the U.S. monetary reserve of less than $11 billion. Considering the hundreds of billions of dollars now circulating, not to mention the more than $100 billion of U.S. short-term liabilities abroad or the $465 billion National Debt, it's hard to think of the dollar as worth anything other than what people (or other nations, from the Arabs to the Zambians) are willing to exchange for it—which, these days, is less and less.

"But the worth of the dollar rests on the strength and productivity of U.S. industry," we are told. Which is true, but inaccurate because—though the U.S. government has the monopoly of the country's currency and can do to it whatever it pleases—the government does *not* have a monopoly over U.S. industries and cannot do to them whatever it pleases. At least, *not yet.* Foreigners are still willing to extend credit to any American capable of producing goods and services; but these same foreigners have not been exactly eager to extend credit to the U.S. government since, shall we say, August 15, 1971, to pick a date a random. Several other governments are in a similar fix, if that's any solace.

What's fascinating is that while various governments have endorsed the mystic notion that wealth is created by issuing billions of little pieces of paper with the portrait of some national hero on it, an increasing number of people are rediscovering gold. In July 1971 the free-market price of gold averaged $40 per ounce. In September 1972, it was $63. In March 1973—a date I remember because I began buying gold coins—gold sold at $84. As this article goes to press, the "price" of gold stands at $176 per ounce.

Where do we go from here?

THE ALTERNATIVES

It might just happen that the next Congress and administration—in some unprecedented attack of rationality and responsibility—will have the courage to rescind a few laws, to cut spending, balance the budget, reduce the balance-of-payment deficit, and lower taxes. Then, if our government could achieve such "miracles," it might even be willing to move toward economic freedom by allowing Americans to own gold and to let them settle their debts with whatever commodity the free market decides. With this scenario, everybody is happy, paper bugs and gold bugs included.

There's another scenario. Without a cut in spending, without a balanced budget, without a reduction in the balance-of-payment deficit, without the legalization of gold ownership, and without a fully convertible standard ("fully convertible" as determined by the free market, *not* by legislative action), there are sufficient grounds to conclude that: 1) the deficits of today will have to be paid via the confiscatory taxation of tomorrow; 2) the creeping 10 per cent annual inflation of today will become a runaway inflation; 3) the controls imposed on the economy "to keep the lid on inflation" will be so draconian as to wipe out the last remnants of freedom and plunge the country into either right-wing or left-wing totalitarianism; 4) the dollar will have no other backing except the military might of the U.S.—and whenever the might-makes-right ideology prevails, the world is anything but peaceful; 5) the combination of any or all of 1, 2, 3 and 4.

Too pessimistic? Well, take a look at South America.

Or, better yet, take a good look at Great Britain and bear in mind that—culturally, politically, and economically—England has invariably given us an excellent preview of coming events in the U.S.

If pragmatism means that people should act according to what "works," and if it's true that our political leaders are "pragmatists," we could make a good case to prove that freedom "works," and that economic freedom depends on gold ownership and real money—not on controls and legal tender—and that when economic freedom is gone, political freedom is dead. But we won't. We are not supposed to know more than our philosopher-kings. Besides, freedom implies responsibility, and to be responsible is to be "square" or "old-fashioned." Our philosopher-kings are neither.

We could point out the virtues of the convertible gold standard by proving that it is incompatible with deficit spending, that it is the most effective defense against inflation, and that it makes the welfare-warfare state impossible. But we won't—and I doubt we *can* because what is a virtue for us may be a vice for *anyone* with vested interests in deficit spending, inflation, and a welfare-warfare state (which includes big business, big labor, and 99 percent of Liberals, Democrats, Republicans, and Conservatives).

"What is a virtue for us may be a vice for anyone *with vested interests in deficit spending, inflation, and a welfare-warfare state."*

We could point out that the monetary system that collapsed in 1971 was essentially the same system that collapsed in 1931—the gold *exchange* standard—a hybrid system which, as economist Patrick Boarman describes it, involved the use of some key currency as a substitute for and supplement to gold in settling balance-of-payment differences among nations. But we won't. After all, that hybrid system of paper and gold didn't work, the International Monetary Fund tells us while informing us that its new hybrid system of paper and "paper gold" (alias Special Drawing Rights, SDR's) will do the trick.

The present and past Administrations have officially maintained that gold is of no importance to the U.S. economy and to government transactions. If that is true, we can then say that there is no logical reason to prevent Americans from owning gold. And that is precisely what most of us have been saying. With some success.

Thanks to Felix Wormser, a 79-year-young libertarian (who's also a mining engineer, was former Assistant Secretary of the Interior under Eisenhower, and is now a director of the Committee for Monetary Research and Education), the 1972 Republican Platform endorsed Wormser's proposal for legalizing gold ownership. Political platforms nowadays are meaningless, you might say. Perhaps. But on April 4, 1973, Senator McClure of Idaho attached the gold-ownership amendment to the dollar-devaluation bill—and the Senate passed the McClure amendment by a vote of 68 to 23.

In 1974, there is a better than a 50-50 chance that gold ownership may be legalized, according to various observers. Perhaps it will.

Meanwhile, what can we do individually?

We can save as much of our skin as we can by buying gold coins. Nothing is riskless, of course, and gold coins are no exception. But they have had a tremendous appreciation in the past few years, and are likely to appreciate at an even faster rate in the future. As other authors point out in this issue of *REASON,* the price trend of common-date gold coins goes along with the price trend of gold bullion.

. . . AND WHERE WILL GOLD BULLION GO?

To answer that question, let's have a quick look at the international monetary mess.

The United States is a debtor nation. International debts can be settled either by a transfer of real wealth from debtor nations to creditor nations, and/or by major political concessions that eventually bring about a drastically altered balance of power among nations.

Let's do some arithmetical masturbation, just for fun.

"To settle both our short-term and long-term debts, the official 'price' of gold would have to increase 20 times to $850 per ounce."

Since there are at least $100 billion of short-term foreign claims against the U.S. gold stock of about $10 to $11 billion, a tenfold increase in the official "price" of gold—from $42.50 to $425 per ounce—would be necessary to meet our short-term obligations abroad. That would merely cure the so-called dollar overhang. But it would not make a dent in settling our *long-term* obligations of almost $100 billion. Thus, to settle both our short-term and long-term debts, which add up to almost $200 billion, the official "price" of gold would have to increase 20 times to an astonishing *$850 per ounce!* Such an event is extremely unlikely: the value of the dollar, be it "fixed" or "floating" or what-have-you, is always related to other currencies (which can be in a worse shape), and ultimately rests upon the confidence that the people of the world have in our ability to master our difficulties. But since that confidence has been severely shaken in recent years, and nothing is being done to bolster it, the relentless upward trend in the free-market price of gold shall continue for a while longer.

Why?

Any government, for "humanitarian," "noble," or asinine reasons, can, in effect, steal freely from its own citizens by inflating the currency. But when it attempts to grab the assets of the citizens of other nations, it is likely to get clobbered. Currency is a claim only against the assets of one's own citizens, who can be forced to shut up and put up with "legal tender" backed with the government's promises and nothing else. But when confidence in a government's promises wanes, *other* nations want to be, and can insist on being, paid in *values*—real goods, real assets, and, ultimately, in gold, not in pieces of paper. No government can tamper with the measurement of value, i.e., inflate its currency, and get away with it indefinitely in the realm of international trade.[1]

When inflation keeps eroding the value of your currency, nations holding your fiat money (say, the Arabs) become increasingly nervous. They don't want the money they are holding to lose value; they don't want to be stuck with your IOU's. They can use a number of tactics to bring you to your senses.

Creditor nations can, for example, drastically curtail their trade with you, and raise all sorts of back-breaking export-import controls. They can unload their reserves of your inflated money into foreign-exchange markets, thus, in effect, forcing you into a devaluation. The latter may be costly to them—but at least they will subsequently be able to make you pay more for the goods you buy from them. Or they can cut you off from their markets. (Would the Arabs have turned off their oil faucets if the dollar had been healthy? Ponder on that sometime.) And, as a last resort, they can send back your paper money and insist that you meet your obligations by paying in gold or, say, a chunk of your territory.[2]

GOLD AND ECONOMIC HEALTH

Gold invariably acts as a thermometer that indicates the health of a country's economic and monetary system. As long as a country is healthy, nothing much happens to the "price" of gold. But when a country's monetary and economic system is in trouble, gold goes up. Plunging a thermometer into an ice bath does not eliminate the fever and does not cure the disease—thus, freezing the "price" of gold at an artificially low level, which is precisely what the U.S. government has done since 1934, is useless.

Actually, it is worse than useless. Because unless you shape up and stop inflating, you'll eventually remain isolated from world trade. Nationalism and mercantilism then take over with a vengeance. Your reserves of foreign currencies and gold melt like snow in July, and you can no longer buy the finished goods or raw materials more economically produced in foreign nations. As a consequence, you are forced to rechannel whatever capital, manpower, and other resources you can muster in such a manner as to produce, at a much higher cost, that which you had formerly imported. Your entire national economy is dislocated; you no longer enjoy the enormous benefits derived from the world-wide division of labor. Very soon, many companies that depended on foreign trade go bankrupt; many people lose their jobs. The price of some commodities (let's say, gasoline) goes into orbit while the price of other commodities nosedives (just watch and see what will

"Any government can steal freely from its own citizens by inflating the currency. But when it attempts to grab the assets of the citizens of other nations, it is likely to get clobbered."

happen to silver and some non-ferrous metals, for instance). Farmers scream their heads off because they can't make a living—they're stuck with megatons of produce they can no longer export (unless, of course, you make a grain deal with Russia, and you know with what results). Many industries that rely on foreign ores are now dangerously short of raw materials—more jobs are lost. Labor unions go on the warpath seeking higher wages and "job security"; demagogues of all stripes have a field day. Profits decline, at first gently; then a trickle of red ink becomes a flood on corporate annual reports. The stock market, which has been going to the dogs all this time, "unexpectedly" crashes. Business and bank failures multiply; millions of people are out of work; the savings of other millions are wiped out overnight.

Sound familiar?

These and similar disasters, lumped together under the category of "The Great Depression," are the phenomena that occurred in the United States and other countries between 1929 and 1939.[3] "It won't happen again." I wouldn't bet on it.

But whatever happens, I am convinced that the nations of the world cannot and will not eliminate gold completely, much as they allegedly dislike the barbarous relic. Why? I asked that question of Jacques Rueff, financial advisor to the French government since the days of Charles de Gaulle. "The nations cannot eliminate gold because, where money is concerned, there is no government on earth that can fully trust any other government," said Rueff, who's a good diplomat and could say no more to me than he did.[4] But since *I* am not a diplomat, I'll put it more bluntly:

Each government is like a small-time crook who periodically writes bad checks. Since all governments sooner or later write bad checks—meaning: since they all issue fiat money—the last thing any government wants is to be stuck with some other nation's IOU's.

At any international monetary meeting, the smiles and polite bows and hearty handshakes are the camouflage for all the savage fighting that goes on in the back-rooms and that is always centered on this one issue: WHO OWES WHAT TO WHOM?

And since they all know that their currencies are fundamentally no good, the issue boils down to: WHO OWES GOLD TO WHOM?

On the one hand, creditor nations want to be paid in gold. On the other hand, debtor nations

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want to settle their debts by writing another bad check, say, a check backed by inconvertible dollars, "paper gold" or Special Drawing Rights. A debtor nation also tries to make gold the scapegoat: it blames the rise in the price of gold for the monetary and economic mess that exists; which is like blaming a thermometer for causing high fever.[5]

Very little gets accomplished at international monetary meetings—except the usual unanimous declaration of eternal friendship, which lasts about three weeks or until the next monetary crisis. Meanwhile, despite the debtor nations' efforts to keep it down, gold keeps on going up. And so do gold coins.

The dollar, says John Exter (a monetary consultant and former senior Vice President of First National City Bank) was convertible into gold until March 1968; up to that time,

> central banks issuing all major currencies were promising all holders: "I owe you gold at $35 an ounce." Under the two-tier system, however, the IOU-gold promise was abrogated for private people, and . . . central banks refused to sell any gold at any price to private people. The IOU-gold-at-$35-an-ounce promise was honored only among central banks and governments. . . . On August 15, 1971, it was abrogated even among central banks. So today all currencies in the world are saying, "I do not owe anybody anything." Each says, in effect, "I owe you nothing in the way of any commodity that is a store of value." Each is an IOU-Nothing.[6]

Since 1968, of course, the various nations have tried to push forth the idea of Special Drawing Rights, as the ultimate answer to the liquidity problem.

But can SDR's work? Again, I quote my good friend John Exter:

> In an IOU-Nothing world, with all IOU-Nothings growing rapidly in number, but more rapidly in some currencies than in others, it is idle for any central bank to think that it can keep the value of its own IOU-Nothings constant, or even nearly constant, in relation to all, or even many, of the rest for very long. So, if anyone thinks that international monetary reform can restore a reasonably stable exchange-rate world he might as well forget it. . . .
>
> I particularly suggest forgetting the SDR. It has no obligor, so it is not even an IOU-Nothing. It is a "Who-Owes-You-Nothing?" If no one promises to pay, there is no limit or check to its creation. The thought of basing an IOU-Nothing pyramid on a Who-Owes-You-Nothing base is not one that a realistic mind can long entertain. [7]

SUMMARY

Monetary history is the history of theft, fraud and lunacy on a grandiose scale.

People can cope with theft and fraud—and they'll be able to cope with some sort of semirational monetary system, such as the gold-*exchange* standard, which will probably be revivified, Bretton-Woods style, along with a temporary relaxation on the prohibition of gold ownership.

Of course, a fully convertible gold standard is what I would personally like to see. I don't know if I will.

But I *do* know that no one will ever be able to cope with the sort of lunacy generated by freely floating IOU-Nothings, or fixed ones, or IOU-Nothings based on 'Who-Owes-You-Nothings.'

Meanwhile, my advice is to get hold of some "metallic SDR's." It's the new name for gold, or will soon be. ◻

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Gold Investments Today: an interview with Donald J Hoppe

Donald J. Hoppe is one of the widest acclaimed authorities on all types of gold investments in the world today. He is author of the definitive and prophetic works HOW TO INVEST IN GOLD STOCKS AND AVOID THE PITFALLS *and* HOW TO INVEST IN GOLD COINS, *which have reached large readerships throughout the world. Mr. Hoppe is actively involved in a plethora of business activities which include his presidencies of Investment Services Inc., and the Numismatic Investment Service, directorships in First Coinvestors Inc. and Aureus Ltd., and a governorship in Rare Gold Management, Inc. He also serves on the Editorial Advisory Board of* INVESTING PROFESSIONAL *magazine and as a private consultant to a Swiss bank. He has also written articles on a diverse set of topics for magazines such as* AIR PROGRESS, MECHANICS ILLUSTRATED, *and* INVESTING PROFESSIONAL. *He contributes to financial newsletters and lectures at financial seminars. Through the years his financial advice has meant millions of dollars in profits and an incalculable sense of well being to those who have heeded it.*

REASON: In the past you have been quite negative about the prospects of U.S. citizens getting back their right to own and trade in gold bullion. Have recent developments altered your opinion on the repeal of the Gold Reserve Act?

HOPPE: Yes, they have. Developments such as the reduction of the Interest Equalization Tax to zero, and especially the Treasury's liberalization of the gold coin regulations, definitely point to a change of policy on the part of the administration. I can envision this repeal by the end of 1974 if the price of gold reaches $200 an ounce. The whole thing is not a question of time, but rather a question of the price of gold, more than anything else.

REASON: Why do you consider that the pivotal factor?

HOPPE: Well, when convertibility can be safely restored to our currency—in other words, when the price of gold reaches a level where we can safely restore convertibility without jeopardizing our gold reserves—then it becomes practical to allow free gold trading in the U.S. For example, if we restore convertibility at $200 per ounce, we will have five times as much gold to sell as we did at $42 per ounce.

REASON: The American public is showing a growing awareness of gold investments. Do you view the recent Merrill Lynch study, which suggested "an exciting future for gold," as a harbinger of an even greater enthusiasm for gold investments on the part of the American public?

HOPPE: When the big brokerage houses begin recommending the gold stocks, the stocks will become respectable. You know you can't sell any stock without sponsorship and, if this sponsorship comes from the big brokerage houses, then sure the golds will become respectable. Of course, this isn't the first time that gold stocks have been respectable. They were very well thought of in the thirties, for instance, when Homestake went from $56 up to $544. This is merely a case of history repeating itself.

REASON: With some observers claiming that the big bull market in gold has only just begun, especially if there are only a few, if any, investment alternatives, can you envision a scramble if investors try to get into the golds at any cost and turn the whole thing into simply a "numbers game," with the public willing and desperate to buy anything that starts with a "G"?

HOPPE: Yes, there is always that possibility. The gold stocks are now becoming the glamour stocks of the seventies as electronics and space issues were in the sixties. However, I don't see the golds selling at a hundred or more times earnings as the aerospace issues did. I do think it is very possible that they could sell at 20 times earnings. Of course, any time you have glamour stocks, you can have very volatile markets with strong price crises; you can have volatile setbacks as well. And the glamour stocks of the past have shown that they can go up a lot further and continue a lot longer than seems reasonable.

REASON: Whenever anyone thinks of the public and the market, mutual funds come to mind. However, almost across the board, the mutual fund industry has been taking a hellish beating. A notable exception would be International Investors, which posted about a 60 percent gain last year with roughly 90 percent of its assets in gold shares. When the word is really out on gold, can you see this and similar funds (several are currently being launched) becoming really popular with the public on a broad scale, or do you think the public is becoming permanently soured on the fund concept?

HOPPE: I don't think the public is soured on the fund concept at all. I also think anything that is new and has glamour about it can be sold to the public and the public will furnish a ready market for gold-oriented funds if they could be sold on that basis. The whole thing depends on how much gold is in the news and how long this gold market continues. Many of the traditional funds are beginning to improve their portfolio performance by buying gold shares. Of course, this becomes a danger because the more the funds get into gold shares the less liquid they become. That is what we're seeing now with old glamour stocks such as the IBM's and Xerox's. When a fund has to get out of one of these, there is no ready market; they can only sell to some other fund. I can foresee a time coming when the funds, for example, will have an enormous position, say in Free State Geduld or President Steyn or some other mining company and when the fund wants to sell 100,000 or 200,000 shares, who do they sell it to? They can't sell it directly to the public without depressing the market.

REASON: Won't this whole problem be compounded by the fact that most mining companies are very thinly capitalized?

HOPPE: That's true, except I think what's going to happen is that as the prices are bid up, you are going to see numerous stock splits and stock dividends so that capitalizations will not remain as thin as they are now.

REASON: Many investors in gold shares are concerned that public envy will force the government to do something about the "windfall" profits of the "un-American" gold speculators. How do you feel about this possibility?

HOPPE: Although I can see this as a legitimate investor concern, I don't think it's probable. It was not done in the thirties when investors made enormous profits in the golds and were not taxed on that basis. If anything, there could be a tax on the profits of the mining companies themselves. On the other hand, I think it would be in the best interest of all governments, especially the U.S. government, to promote the production of gold for our monetary reserves. I said a long time ago that when this crisis came, the government would shift its position from restricting to encouraging the production of gold, and I think that we're seeing that happen today.

REASON: There are also those people who are worried about actual confiscation of gold shares, particularly South African shares held in the form of American Depository Receipts (ADR's). What advice do you have for them?

HOPPE: This is always a possibility, since we simply don't know what idiocy the government can think up next. But, it looks to me like the present thinking is to encourage investment in foreign shares, as evidenced by the reduction of the Interest Equalization Tax to zero. I really don't think they have any plan for confiscating these shares, although other countries have tried it at other times. If you are worried about confiscation, the way to get around it is to have your ADR's transferred to International Depository Receipts (IDR's) by the Morgan Guaranty Trust or whoever is the custodian for your ADR's. The IDR is a bearer certificate that can be negotiated anywhere in the world. It's not made out to you personally, but rather, it is a certificate that can be readily negotiated in any currency at any time and any place. For some reason, the banks are reluctant to give out advice or to make public the fact you can change ADR's into IDR's. If you're interested in this change, contact the registrar of your ADR certificates.

REASON: With recent and massive increases in the price of petroleum, there is a great deal of speculation as to what the Arabs will be doing with their new-found liquidity. With the growing paucity of alternative investments and currencies, can you see the OPEC (Organization of Petroleum Exporting Countries) nations making a real run for the bullion vaults in the near future?

HOPPE: I think what the Arabs want is a convertible currency. As the Oil Minister of either Kuwait or Dubai said recently, "We have been selling our oil for currency of doubtful and changing value," and until the West got together and decided what the value of their currencies would be, he didn't see the sense of selling us any more oil. I think that's an understandable position. Let me add that the Arabs are going to ask for, and eventually will not sell oil without receiving, either a convertible currency, convertible currencies, or else gold. Whether it is a convertible

dollar or a new convertible Eurocurrency, I don't know, but they will demand, and will have to get some form of convertible currency which has a fixed, measurable value that they can trust.

REASON: Some market traders have been looking for a "Petroleum Rally" when the oil embargo is lifted. What are your feelings on this probability, and on the general state of the market itself?

HOPPE: The market is currently poised for some sort of rally and certainly the lifting of the embargo could trigger it. But a rally is a rally and not a bull market. I think some fundamental changes will have to be made before the foundation for a new bull market can begin and we're nowhere near this point now. On a cyclical basis, we possibly could have a new bull market beginning in late 1974 or early 1975, but it is too early for this to be more than a rally. To have a sustainable bull market and a new wave of prosperity, we must have a fundamental solution to the international monetary problem. Now this solution may not last for more than a year or two, but at any rate, they will have something that everybody believes is a workable solution. For example, when the two-tier market system for gold was adopted, in 1968, this was thought to be a workable solution to the degree that it created a bull market that lasted over a year. Now perhaps, we will be getting another interim solution that could be compared to the two-tier market, which was not really a solution at all. But it was psychologically sufficient to lay the foundation for a new bull market in the stocks. The officials at the Treasury and the International Monetary Fund are enormously creative in coming up with stop-gap measures to postpone solving these problems. Of course, this just makes the ultimate solution all the more difficult, but nevertheless, they may come up with something. Yes, very definitely, lifting the oil embargo would be a temporary short term stimulant for the stock market and a temporary short term depressant for gold shares and probably London gold.

REASON: How do you feel about the way the price of gold has been behaving recently?

HOPPE: If you look at the chart of the London gold price, you see that it is going exponential. Where it will all end, I don't know; I would say a minimum of $180 to $200 per ounce, just based on the chart as we see it today. The whole situation is very complex because we are trying to determine the future of literally dozens of world currencies, which will all have their effect on the price of gold. In order to see the top in the price of gold, we will have to see a bottom in the value of the currencies, specifically the dollar, and I don't see any bottom to the dollar at the moment. I don't know of any sound, solid evidence to forecast that the dollar is going to stabilize at any particular level. In other words, as long as we have our present economic and political philosophies of managed money, I don't think there is any limit to the depreciation of currencies. Until we change our whole economic and political philosophy, I think we will have continuous inflation.

"I can envision repeal of the Gold Reserve Act by the end of 1974 if the price of gold reaches $200 an ounce."

REASON: Since Homestake is the most important gold mining property in America today, I'm sure our readers would appreciate some of your observations on the investment potential of this company.

HOPPE: I've been a bull on Homestake in the past and I still think it has a bright future. The company also has an interest in lead and zinc production, in addition to being the largest gold producer in North America. I like the management of Homestake and think the real future will be if they can get additional gold properties. The Lead, North Dakota, mine is still a viable property. They have recently opened up the mine down to the 8,000 foot level and there appears to be ample ore reserves for operations well into the future. The only drawback with Homestake is that only about 40 percent of its current income is being produced by gold. Of course, as the price of gold goes up, this proportion will undoubtedly increase.

REASON: Homestake is known for its volatility, so could you give us some guidelines for properly buying the stock?

"I really don't think the government has any plan for confiscating foreign gold shares, although other countries have tried it."

HOPPE: As to where to buy Homestake, I think we have to go on an earnings basis. Homestake just announced their earnings for the past year at about $3.70 per share, which means the stock is currently selling for more than 1973 earnings. I think there is a fair chance we'll see 1974 earnings in the neighborhood of seven dollars or more. At 20 times earnings that would bring the stock up to a price of $140 or more. Whether you could sustain the 20 times earnings valuation for Homestake, I can't say, but I do think with the fund and public interest in the golds the way it is, that a 20 times earnings figure could stay for quite a few years. I want to mention here that during the great boom in Homestake shares in the thirties, the PE ratio on Homestake never rose above 10, but you see, times do change.

REASON: How do you feel about the major Canadian mines such as Campbell Red Lake, Dome, and Giant Yellowknife at this time?

HOPPE: In the Canadians, I think the situation is analgous to what we have with Homestake. We have to judge the merit of those stocks based on their earnings and the multiple people will attach to their earnings. Campbell Red Lake is selling around 20 times earnings at present and Dome is around 40 times last years earnings and about 20 times potential 1974 earnings. If you assume that Dome made better than $6 per share in 1973 and it is now selling for $180, that's a multiple of 30 based on 1973 earnings. We can anticipate that 1974 earnings will be $12 per share, and in that case, it is only selling at a nominal 20 times earnings. At this point, I would be inclined to buy Campbell Red Lake and Dome as trading stocks and to pick these, whether for investment or trading, on the reactions rather than the bulges because I think they are generously discounted at 20 or 30 times earnings. However, we don't know to what multiple the public will eventually drive them. But there is a scarcity factor with gold mines, so who knows—maybe we could see Homestake, Dome, and Campbell Red Lake selling at 50 times earnings.

REASON: Some of the South African mining finance houses have not been performing as well as some investors expected, or would have hoped since this past September. How do you feel about the whole question of mining houses in a gold portfolio?

HOPPE: Not all the mining houses have performed badly; Goldfields of South Africa, Centrust, and Johannesburg Consolidated are among those that have performed very well. The criteria I think you have to observe in buying a mining finance house is the percentage of gold in their earnings and assets. Obviously those with very small percentages of their assets in gold have not profited from the gold boom. But there are some houses that have anywhere from 45 percent to 80 percent of their assets and earnings in gold. Part of the reason the houses did not participate to some extent in the gold boom and were tardy in their upward moves was because there were some forced liquidations of these stocks by the London brokerage and banking communities. The London financial community was in a lot of trouble last fall and was selling these shares off for liquidity. Last fall, I did recommend buying the mining finance houses because I knew they had been depressed to absurdly low prices, and since then, they have come back rather smartly. But if you want to play a finance house, get one that has at least 40 percent or more of its assets in gold.

REASON: For those people who have been in gold stocks for a time and who have experienced large capital gains, would you recommend taking a portion of their profits and working them back into mines that are in the process of acquiring longer lives and

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perhaps have yet to experience large premium runs?

HOPPE: Possibly a portion, but certainly not all because I still think that the basic holdings in the portfolio should remain the long-life and higher quality mines. This is a case where you must differentiate between speculation and investment. For investment purposes, long-life mines such as Kloof Vaal Reefs, West Driefontein, and Western Deep Levels, should be the basis of your portfolio because they will survive no matter what happens to the price of gold. For example, a retreat of the price of gold back to the $100 level would still allow a West Driefontein and a Western Deep to keep operating but would have serious effects on, say, East Rand Proprietary. Since we don't know ultimate outcomes for sure, safety should be the ultimate criterion. On the other hand, according to my calculations some of the highest leveraged mines are East Eriefontein, Hartebeestfontein, Ellsburg, and possibly South Vaal and Randfontein, which I have had in my high quality stocks listing, so the leverage is not always in the low quality issues.

REASON: To what degree do you weigh potential or actual income from uranium as a by-product of gold mining when you evaluate a property such as Vaal Reefs?

HOPPE: I disregard the value of the uranium entirely. In the past decade or so uranium has been a bear market with the actual consumption of uranium below expectations. I'm not that knowledgeable about what the future will bring as far as the uses of uranium, but it wouldn't surprise me a bit to see it by-passed in favor of some more radical form of energy. Earnings from uranium don't particularly impress me; they are nice if you have them, but the mine certainly should be capable of surviving without them.

REASON: In addition to gold, platinum and shares in platinum companies will occasionally be touted as an effective monetary hedge. Do you feel there is any place for a platinum commitment in an essentially all gold portfolio?

HOPPE: Platinum, like silver, is strictly an industrial commodity and, unlike silver, is one of the precious metals that is currently in oversupply. Even discounting its use in auto emission controls, there is still an oversupply. I'll grant you that in a severe inflationary situation almost anything you can get your hands on is a hedge (say copper and zinc) but I don't think the platinum market is liquid enough, and I would confine my actual metal holdings to gold coins and perhaps some bullion if it is allowed, and let the platinum investments go by.

REASON: I understand you are negative about silver for investment purposes. Could you please explain why?

HOPPE: I'll grant you that silver is probably an inflationary hedge in the fact that it is the poor man's gold and someone can establish a position in the metal with just a couple of dollars. However, I feel there are two important things going against silver; first, silver is an industrial commodity and in the case of a slowdown or depression in the economy, its price will drop. Second, if and when the public is allowed to own gold bullion, there will be a lot of switching out of silver into gold. I don't like the way the silver market is behaving at this time and personally regard the whole thing as too speculative.

REASON: Your predictive abilities in the past have almost verged on the uncanny. I'm sure our readers would appreciate your thoughts on what type of economy we are going to see in the next several quarters, and where you think the price of gold is heading?

HOPPE: I predicted in the early part of 1973 that there would be a recession starting in the first part of 1974. This was before the oil crisis became apparent which of course will make this recession even more severe. I also predicted a recovery in the final quarter of 1974 or the first quarter of 1975. As far as the price of gold is concerned I'm looking for a possible $200 by the end of the year with a minimum of $160. For the long term we don't know where the bottom of the dollar is, so we don't know where the tip of the gold price is—although we might see $300 gold by 1976. I think we are in a long term bullish trend in gold and I see no sign that the bearish trend on the dollar is ending, so I would suggest that you stay with the major trend.

REASON: I understand you are thinking about writing a third book. Would you give us a preview?

HOPPE: I'm thinking about writing a book on the general theme of money, gold, and freedom because I feel that sound money is essential to political freedom. I think there is a very direct relationship between money, gold, and freedom, and I would like to put that in historic perspective and comment as to what I think ought to be done to prevent a loss of freedom from occurring in Western civilization. I don't think even today people realize what a threat it is to our whole way of life, to Western Civilization, to capitalism, to human dignity, and freedom to have lost control of our monetary system. Unless we restore sound money, the free market economy cannot survive and I would like to be very forceful in pointing that out. ◻

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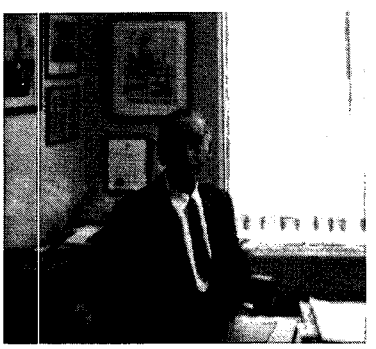
SILVER: no longer "poor man's gold"

Henry Banzhaf

The accelerating price rise of the last nine quarters has taken silver out of the "poor man's gold" class. The abundant supplies and low prices of even 15 years ago are gone for good.

Silver and gold are metals with unique metallurgical qualities in an equally unusual combination. No substitute as yet exists which can approach their advantages when used for ornamental art, money or certain small-unit, high-volume industrial applications.

Silver and gold were used for money and artwork at least as early as 3500 B.C. in Egypt, Chaldea and probably China, more than 2000 years before the Bronze Age, the glory years of the Cretan civilization. As money, silver was more frequently used than gold because there was more of it, and lying close to Earth's surface it was more easily found. For example, the coinage of ancient Athens was silver. About 400 B.C. Aristophanes described the bitter comment of an Athenian as he contemplated the future of his "good silver drachma" recently alloyed with copper, an early, but far from the earliest, victim of currency debasement by an over-extended government. Today, even our copper pennies, hoarded by the public at a faster rate than the mints can produce them, are about to be made of aluminum.



Henry F. Banzhaf was graduated from the U.S. Naval Academy, and served with the Navy during the second World War. He has held functional and general management positions in the manufacturing industries. In the past 12 years he has engaged in general management consulting, the last 9 years with his own firm. Since 1966, his work has been concentrated on investment management for a limited number of clients. He conducted the Silver Workshops at the International Monetary Seminars held in Bermuda (1971) and Montreal (1973). He is a licensed Professional Engineer and Investment Adviser.

Not often in an individual's lifetime do outstanding opportunities for long term investment occur, unrecognized by the great majority of investors. By 1970, however, the cumulative effects of rising U.S. inflation rates and their spillover into the economies of the other major industrial nations became increasingly apparent. To the few who did their homework carefully, it was clear that accelerating inflation at home and dollar devaluation (in terms of gold) abroad were sure to come in the near future. A strong, long term rise was bound to be ahead for gold and gold-related assets, while the future of the stock market over the next five years was loaded with risk and uncertainty.

Because of its normal price ratio (16:1) to gold, as well as its historic monetary role as a store of value, silver is a gold-related asset. By 1971, its technical characteristics, price insensitivity to both supply and demand forces, the production-consumption deficit and the end of U.S. government sales started silver on a strong, long term rise. Exhaustion of U.S. government inventory in 1970, the impending end of noncommunist private stocks by 1975-76, and an above-normal price ratio to gold brought the leverage on silver to a point theoretically greater than on gold. Bullion, silver coins and the shares of good silver mines were as good as and possibly better than gold for long term appreciation.

SILVER HITS BOTTOM

The two year decline in the spot silver price from the mid-1968 high of $2.56/oz. to the 1970 low of $1.57 had discouraged many investors. They were familiar with the production-consumption deficit, and knew little and cared less about the monetary roles of silver and gold. Most of these investors abandoned their positions with substantial losses, especially those in the futures market on thin margins. In the last half of 1971, a series of random events, short term in nature, occurred almost simultaneously. The remaining weak holders of silver assets

sold out or were forced out. Meanwhile, the first drawdown since 1965 on private bullion stocks on the New York Commodity Exchange was made. The weekly Treasury sales to industrial users, which had kept private stocks largely intact after 1965, had ended in November 1970 on exhaustion of Treasury inventory.

The stage was set for solid, strong, long term investors in silver assets. The fourth quarter 1971 low of $1.28/oz. provided one of those rare opportunities to increase existing investments or initiate new ones. At the same time, a torrent of antigold propaganda from Washington depressed the free market gold price slightly and gold shares more severely. Investors in gold-related assets had the same unusual opportunity as silver investors to add to previous commitments and make new ones. Since then gold and silver bullion, coins, and shares have increased by about two and a half to five times.

Now (early 1974) investors with no gold or silver holdings wonder if they've missed the bus by failing to protect their assets from inflation and dollar devaluation. The huge increase in world oil and gas prices adds another kicker to already dangerous inflation rates in the major industrial nations whose economies have been based on abundant, low-cost energy.

This situation, on top of seriously strained financial structures in the Common Market, Japan, and especially the U.S. will cause balance of payments deficits, increased destructive inflation rates and slowing economic growth in all of these nations. No one of these three factors has occurred at the same time in all major, industrial countries prior to 1970 when world inflation began to get out of hand. Now, for the first time in history, all three problems will plague these governments simultaneously. The impact, particularly on the U.S., compounded with already critical financial fundamentals, will be immense. Under these conditions we expect gold and silver prices to rise. Gold will move to $200 per ounce, perhaps higher, this year. Silver's advance in February to a spot price of $6.70 may be its high for 1974. Its price has doubled since year-end. In addition to uncertainty about Congress's action on the bill to sell 117 million ounces of the remaining 139 million in the strategic reserve, India's recent repeal of its law forbidding the export of silver raises the possibility of increased supply. We will review this in more detail later on.

By the end of this year, or early next year, *unexpected* deflation should be apparent in the U.S., and probably other large industrial countries. This development should cause a sharp drop in silver and probably gold prices. The Common Market and Japan will fight for their overseas trade. Competitive devaluations, already begun, will increase.

Against this emerging change in the world's principal economies, we believe that gold shares are still in an early phase of a long term rise as bullion prices continue to increase. Gold mining companies will need at least a year after the gold price peaks to adjust operations to maximize earnings. Carried along with gold and impending scarcity, silver and silver stocks should also have a bright future over the next few years.

"By the end of this year, or early next year, unexpected *deflation should be apparent in the U.S. and probably other large industrial countries."*

However, toward the end of the year as deflationary evidence mounts, silver's price will probably fall, especially if the Congress votes to sell the proposed 117 million ounces from the strategic stock pile. The price drop should be sharp, probably aggravated by bullion dealers' transactions. The reasons will be largely emotional. In prior recessionary periods, a demand slump caused severe price declines. The conditions which produced this result won't be around now, and silver's fundamentals will continue to be strong. Nevertheless a Pavlov reaction is likely to occur. Investors should be prepared to reduce silver investments in this event. If a substantial price drop actually occurs, a great buying opportunity will be at hand.

SILVER IN THE RECESSION

Any uncertainty about the short and intermediate term price levels of silver centers on five questions. *First,* in a recession will a contraction in demand cause a serious price depreciation as has been true in the past? In the case of silver we believe it will not, this time. The demand factors are as follows. Noncommunist world consumption in 1973 increased again to 483 million ounces, up 13 percent compared to 1972. Of this, industrial demand was 463 million ounces, up 18 percent, and coinage 20 million ounces, down 45 percent. Use of silver coinage had risen steadily from 1970 through 1972. The drop last year we believe temporary, and coinage should rise substantially again this year. U.S. industrial demand rose to 190 million ounces, up 26 percent and accounted for 41 percent of total industrial usage.

The total shortfall between total noncommunist production and total consumption was 234 million ounces in 1973, 184 million in 1972, 133 million in 1971, and 110 million in 1970. The gap was made up from 1971 on by drawdowns from private stocks, U.S. Treasury coinage, stocks of foreign governments, demonitized coin, smuggled silver from India and salvage.

Withdrawals from private reported and unreported bullion stocks, not counting supplies from India, were 90 million ounces in 1973, 95 million in 1972, and 55 million in 1971. The latter year was the first for such drawdown since 1965. In that interval, U.S. government sales made up the difference plus adding to private inventories. About two-thirds of the difference between total production and total consumption, on the average, is made up from secondary sources and the rest from private stocks.

Among the components of demand, the photographic, electrical and electronic, and commemorative and collector arts categories each hold about 25 percent of the market for a total of 75 percent. Usage in commemorative and collector arts doubled in 1973. We expect this market to remain strong as purchasers increase hedging against inflation. Photographic, electrical and electronic demand, we believe, will fall this year as deflationary forces develop.

Total noncommunist world demand should drop about 15 percent. Allowing for a modest increase in primary mine production and a drop in by-product silver from copper, lead and zinc, we estimate a two percent rise in total new production. The end result should be a reduction in the withdrawal rate from private stocks. However, in view of the rising gold price, continued monetary uncertainties, widespread distrust of currencies, and scarcity not far off, sales of inventories will be at historically high prices. And while usage reductions in two of these major use categories will occur, the use of silver in new applications—bearings, brazing, batteries, electrical contacts and circuitry, water purification, x-ray film, detergents, catalysis and petroleum additives—will help to offset the decline.

SILVER SUPPLIES

On the supply side world production rose four percent in 1973. There are five major sources—

(1) *Mining*—primary silver mines produce only around 13 percent of total supply. At current prices, an annual increase of two percent may be expected. In three to five years as new mines—they will be few and small—begin to produce, annual growth should rise to three percent, but by then private stocks will be almost gone except for carefully tended hoards.

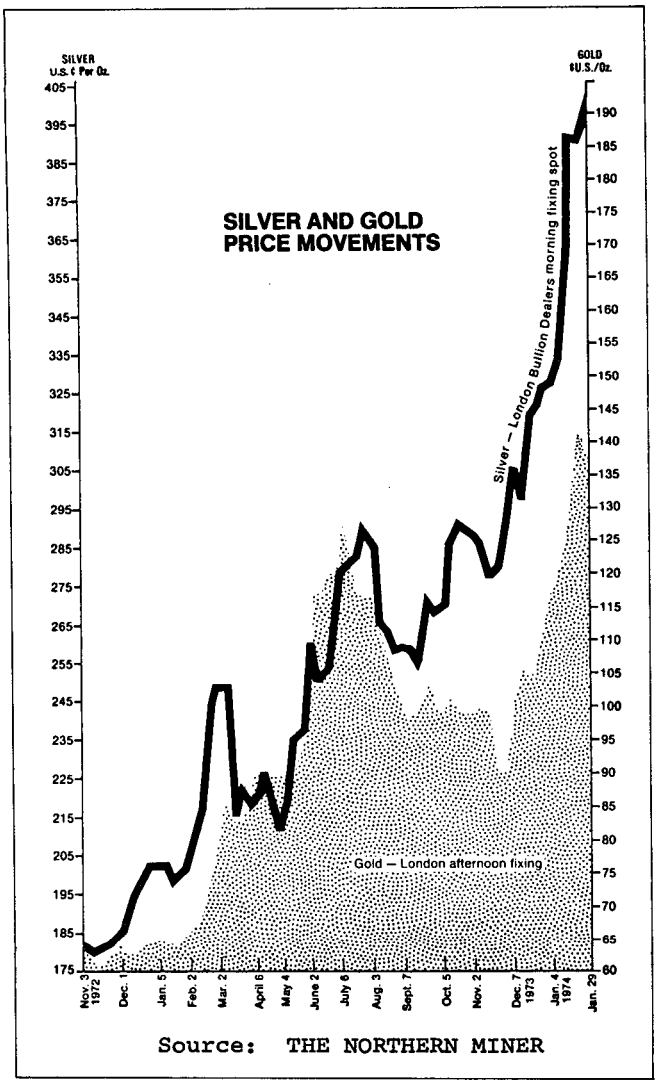
About 39 percent of total supply is by-product silver from copper, lead and zinc. These metals are the first to suffer in a recession. Their production will drop faster than silver demand. Salvage by recycling of all three base metals without any silver byproduct will increase. On balance, silver demand will drop less than silver production. In past recessionary periods, a huge silver inventory overhanging the market pushed prices down. Now most of these stocks are gone. And 40 years ago, there was small industrial demand.

"Finally fed up with base metal coinage and fiat money, the public each time restored 'hard coins' and gold or silver-backed paper."

(2) *Secondary sources*—these include salvage and sales from India. Since 1969 salvage has risen steadily from about 15 million to about 56 million ounces. As silver prices rise, opportunity for increasing salvage improves. Still we think this rising trend will continue to flatten out as it has since 1972. Most of the technical progress in recycling silver has been made, and further advances will be gradual. In a recession, silver salvage will decline with demand.

Indian silver has long been one of the two major threats often reported by silver bears. It's true that India holds large amounts of silver. Nobody, including the Indian government, knows how much. The February ending of its law prohibiting the export of silver probably was motivated by Arab requests for payments for oil in gold and silver. Perhaps another reason may be pressure from western governments.

If the Arabs take silver bullion directly in payment for oil, they will probably store the silver and it will not be available elsewhere. If India sells silver for foreign currencies, the silver supply will be increased. However, their supply of bullion is small compared to the total amount. Most of the silver is contained in jewelry and religious objects tightly held by individuals who regard silver as their ultimate security. The chances of any release, even at present prices, is less than even except in some personal



Source: THE NORTHERN MINER

emergency like the famine of 1968. The government will have to find, persuade or order, and then refine the metal.

By 1972 smuggled silver dropped to 6 million ounces. Higher prices in 1973 brought this amount to about 26 million ounces, within our estimated range of 25-30 million. It's been estimated by some that the end of export restrictions will produce 200-300 million ounces from India. We think the wish is father to this thought. Nobody will have a standard of measure until at least the end of this year. We think these exports may reach 40 million ounces annually. If they are sold for foreign currencies instead of directly for oil, this should have a mild, retarding effect on silver's price rise.

The second scare story frequently used by the bears is a new photographic process eliminating silver. Officers of Eastman Kodak periodically deny this story, but it's still around. We think there will be developments that gradually reduce the use of silver in a few areas, but this will be limited in application and the impact small. The difference will be more than made up elsewhere.

(3) *Coinage*—it's been estimated that the potential supply may be two billion ounces. No one can be sure. Quantities of demonitized coin fell from 50 million ounces in 1969 to 15 million in 1972 and 1973. Recently the volume increased when U.S. coins sold at a discount from spot silver prices. The U.S. coin melt rose three million ounces in 1973 from 213,000 ounces in 1972. World coinage melt will probably increase this year by 5-10 million ounces.

(4) *Government Stocks*—these stocks now total about 250 million ounces, mostly in the U.S., Mexico and India.

In 1946 the U.S. government held nearly 2 billion ounces. Although a large net importer, the government rapidly sold off its supply first at $0.91 per ounce, then at $1.29 and finally at the market price down to zero inventory in 1970. From 1964 through 1970 alone, the Treasury sold 904 million ounces. Thus like gold, our huge stock of these increasingly scarce, store of value assets have been sold off at bargain basement prices.

Today most of the remaining total government stocks will be held for military reserves and coinage. Except for the possible sale of 117 million ounces from the U.S. strategic reserve, we expect sales to decline from last year to about 25 million ounces and to continue that trend.

(5) *Private bullion stocks*—these include industry stocks plus the reported stocks of the London, New York and Chicago commodity exchanges. Also included are unreported stocks held in the U.S. and abroad, excluding communist countries. Their values are estimated. The total is put at about 200 million ounces. We estimate minimum working inventory, including the hard core hoarders, at about 80 million ounces, leaving a balance of 120 million ounces in strong hands after the 1971 shakeout.

The best thermometer for the silver temperature is total inventory at New York, Chicago and London. At the end of June, 1973 these stocks were about 90 million ounces compared to December 31, 1971 at 130 million ounces. By November of last year there was a further drop. But at year end, the total rose to 108 million as shorts rushed silver to New York to meet December contracts for unexpected delivery of 20 million ounces to Texas investors. By February total stocks resumed their decline to 105 million ounces.

Balancing our estimated fall in world consumption in 1974 against our estimated supply, there will still have to be some liquidation of private stocks, assuming the U.S. government does not sell the proposed 117 million ounces from the stock pile. With private stocks strongly held, reinforced by world monetary pressures, rising gold prices, and a "scarcity premium," any price decline will be largely emotional rather than fundamental. Such an event would offer a buying opportunity. Assuming a future average 50 million ounce per year depletion rate in world stocks, these inventories would be down to minimum working levels in two and one-half years.

MELTING DOWN COINS

The *second* major question is whether old silver coinage will come to the melting pot in amounts large enough to have an important effect on the price. While potentially this is possible, as a practical matter we don't think so. We believe that no more than about 300 million ounces will ever be melted. In 1973 total demonetized coin was about the same as in '72. Recently U.S. coins have been selling at a discount from the spot silver price making it practical to absorb the melting cost. Coin melt has increased. Still, until the forward premium disappears, we think release from this source will be gradual. Probably silver from demonetized coin will increase this year another 10 million ounces to total 25 million. We don't expect the coin melt to be large enough to effect the fundamentals for at least three years.

Third, will Congress approve the Administration's proposal to sell off its strategic silver reserve for income—a move, in our view, comparable to a once wealthy individual disposing of the family jewels to maintain his unrealistic standard of living? Such action would include 117 million ounces of silver of the total remaining reserve of 139 million ounces. We believe that the entire reserve is already so inadequate that only a part, if any, of this amount will be sold.

"During the next three to five years the gold-silver price ratio will not only return to its historic value, 16:1, but possibly go below it."

During the first World War the U.S. government had to use 350 million ounces for international payments, because suppliers questioned the currencies of belligerent governments. In the second World War 900 million ounces were used for the same reason. In 1965 the Defense Department, we understand, asked for a minimum silver reserve of 500 million ounces. Now a small Treasury reserve for coinage, about 6 million ounces in the Defense Department, and the 139 million ounce strategic stockpile is all the government has left of a rapidly disappearing, almost irreplaceable asset.

However, if the 117 million ounces are all sold, the amount would be used in 12-18 months. There would be a psychological impact on the price. We think the reaction low, considering world monetary conditions, could be $4.00.

SILVER AS MONEY

Fourth, is silver money? For centuries there have been repeated attempts to demonetize gold and silver as governments sought to pay for extravagant policies through inflation. Every attempt has failed, and we believe present attempts will also fail. Finally fed up with base metal coinage and fiat money, the public, or a new government in to clean up the mess, each time restored "hard coins" and gold or silverbacked paper. Recently, the head of the Bank for International Settlements, the Common Market clearing house bank, stated that gold will remain in the monetary system at higher prices. He referred to S.D.R.'s (paper gold) as without value, and declared gold as the only monetary asset guaranteeing monetary authorities independence from political interference. All this is contrary to what we hear from Washington.

Over 5000 years ago these two metals were selected as "money" because of their unique combination of qualities. As a medium of exchange and standard of value, both metals were used with balancing scales to measure weights of items offered for sale whose values were expressed in terms of silver or gold. The metallurgical characteristics that led to their selection then are the same today. Thus the reasons for the original choice of silver as money are not subject to change simply because silver is not now a currency reserve or generally used in U.S. coins.

Recently this point has been emphasized by a proposed revival of the ancient practice of selling materials against a measure of gold or silver. The Arabs have proposed partial payment for oil in these metals.

Silver coinage is again beginning to increase, largely because of public insistance. In 1969, 64 issues were minted by 28 nations. In 1972, 78 issues were minted by 41 nations. Total noncommunist government gross silver revenue (total face value of all world coins divided by total ounces of silver minted) was $3.53 per ounce in 1969, $4.88 in 1970 and $6.90 in 1972. In three years, the monetary value of world silver coinage increased 95 percent.

During 1973, however, world coinage dropped 45 percent to 20 million ounces. We believe this is an abnormal decline. 1974 will see a return to rising usage. The Canadian government has announced an 11 million ounce sterling issue with 50 million ounces to follow. The U.S. has authorized 60 million 40 percent silver coins for the U.S. Bicentennial, 45 million to be minted by July 4, 1975.

THAT OLD 16:1 RATIO

Fifth, is the historic 16:1 price ratio of gold to silver dead? The value link between silver and gold has existed for over 5000 years, as long as silver and gold have been considered money. No combination of national rulers, finance ministers or economists has been able to shake the tie. In the beginning the ratio was small, 2.5 to 1. But in the fourth century B.C., a 15 to 1 ratio was established that lasted till 1874 when the U.S. changed the ratio slightly to 16:1. The 1890 discovery of the Comstock Lode, a huge silver strike now mined out, during a period of small industrial use, increased the ratio to 40:1. However, the 16:1 ratio reappeared from April

to September, 1968 when for the first time in over a century there was a free market price for both metals.

In our opinion, silver is still cheap relative to gold. At current prices the ratio is about 30, far above the normal 16 existing for 23 centuries until recently, but down from about 46 at the end of June 1973. During these centuries, however, there were swings around the norm. As long as the gold/silver price ratio was constant, silver was as good as gold as a currency reserve. But since the ratio wasn't constant, in 1867-74 silver as a monetary reserve ended

"Recent silver price increases reflect increased unofficial monetization of silver by private owners."

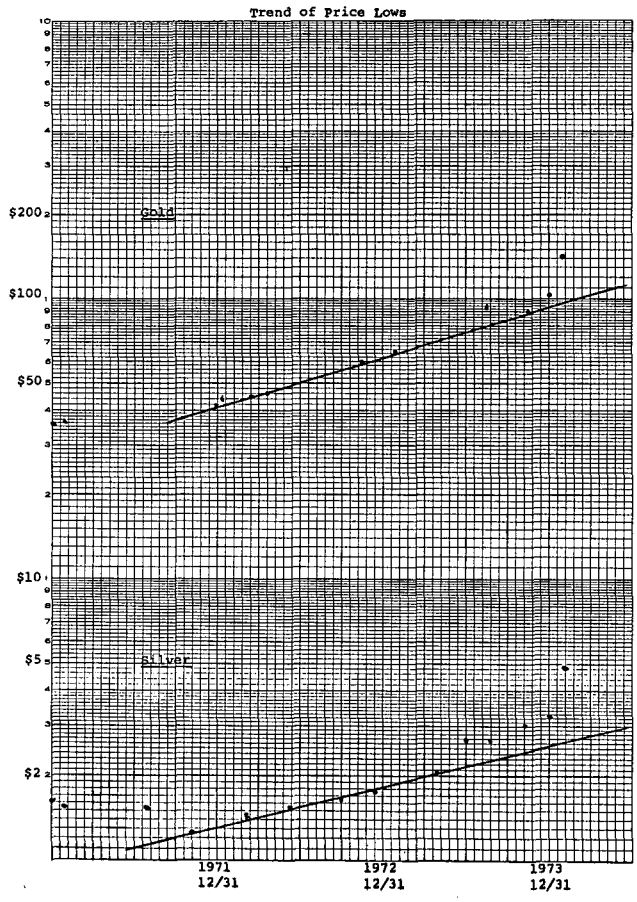
in Germany, the U.S., Sweden, Norway, Holland and Japan. India joined the others in 1893, though in all these countries the use of silver coins continued.

Assuming that gold will reach $200 per ounce this year, and using last summer's high price ratio of 46, silver should be worth $4.35. By last February the ratio had substantially closed the gap and declined to 30. Applying this ratio, twice the long term average, silver should reach $6.67, the approximate year's high already achieved in February. The average ratio of 16 brings the price to $12.50. This year, uncertainty regarding action by Congress and the Indian government should tend to retard the rise in silver's price. Until these factors clear, we think $6.00 is a good target for silver in 1974.

The reasons, we think, for these abnormally high ratios are a growing concensus that silver no longer has a monetary value, and loss of confidence resulting from the severe, unexpected price drop in 1971. The inventory overhang that caused the 1971 price collapse is practically gone. We believe that the majority opinion which refuses to accept silver as money and considers the silver-gold value link dead will change. The result will be a gradual decline in the ratio, as it has in previous, similar periods.

The ratio chart, showing the rate of price change, compares the rising trend of price lows since 1971. The trend lines are nearly parallel, showing that bottom trends are rising at about the same rate. But since the second quarter of 1973, the lows of both silver and gold are rising above the trends at roughly similar, increasing rates, exponentially. This indicates a high probability for still higher prices ahead.

We think that during the next three to five years the gold-silver price ratio will not only return to its historic value, 16:1, but possibly go below it. Assuming the government's silver reserve stockpile is not dumped on the market, this year should see a hard squeeze on the shorts. Continuing monetary



uncertainty, rising gold prices, and approaching scarcity will probably slowly turn private owners from sellers to holders and buyers. On the numbers, it's probable that silver's price will increase more than gold's.

Recent price increases reflect not only continued demand by industrial users, but also increased, unofficial monetization of silver by private owners. We think their objective is less for short term trading than for long term protection against rapid money depreciation.

Most buyers of silver bullion are British and American because they cannot legally own gold. It is assumed that if Americans were to be permitted to own gold, silver holders would switch from one to the other. This may happen in a minority of cases, but because silver is still historically cheap compared to gold and the scarcity premium is not far off, the majority of silver holders, we think, will stand firm, anticipating the rewards of superior leverage.

Although silver stocks have risen substantially, the shares still lag the bullion price. They are, generally, in the early stage of a long term rise. By taking advantage of temporary reactions, and especially the setback that should occur if the Congress approves the proposed sale of silver from the strategic reserve, the securities of good silver mining companies and silver bullion should be outstanding long term investments. ◻

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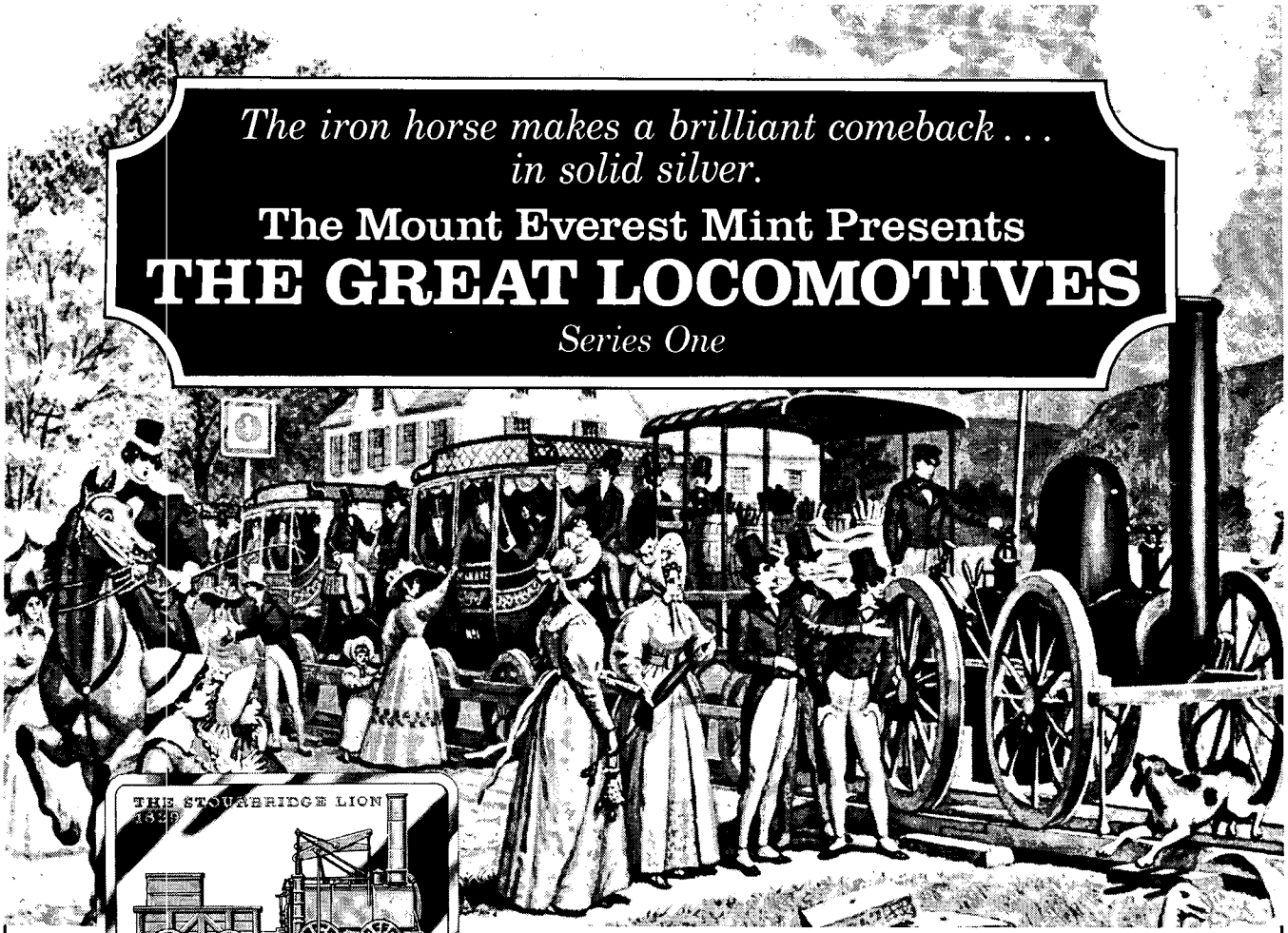
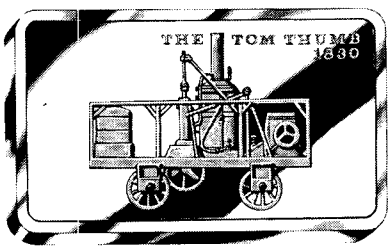
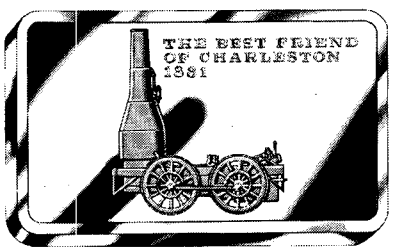
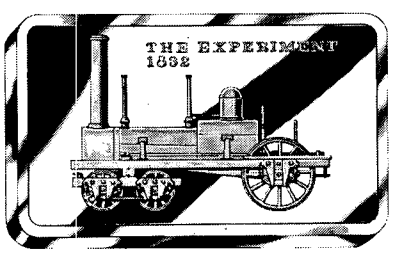
THE GREAT LOCOMOTIVES

Series One









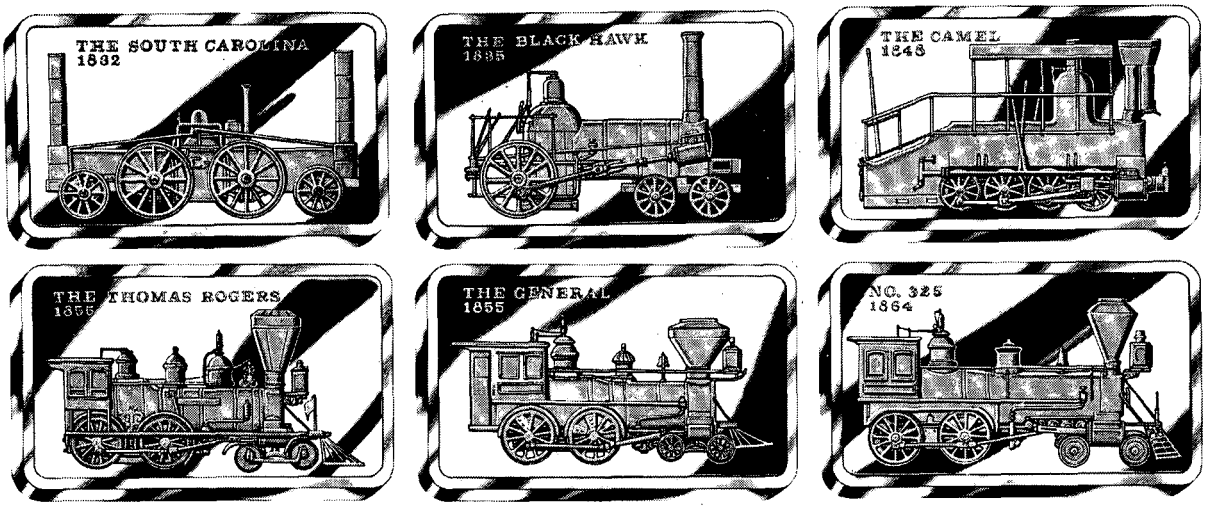
- **A series of ten commemorative silver bars. Includes the most historically significant locomotives in American railroading's first 35 years.**
- **Absolute limit of edition will be 5,000 sets.**
- **You can build this set in a most reasonable manner — by acquiring only one bar per month.**
- **Each bar will be a frosted proof, serially numbered and registered, to certify the subscriber's ownership.**

Railroads are coming back — to help us travel during the energy crisis. (They're bringing together people who used to ride alone.) Railroading is making news in 1974.

Silver also is making news. More people are collecting it — to protect themselves in the present inflation crisis. (After climbing 75% in 1973, the price of silver is likely to rise 52% from today's level — in 1974. This prediction was published by a very conservative and very accurate economist.)

Art is another popular vein of appreciation. In fact, Japanese and European entrepreneurs have become the high bidders at recent auctions of limited edition American art. It has appeal from country to country to country.

With the foregoing trends in mind, The Mount Everest Mint brings all three together in a first-of-its-kind series: THE GREAT LOCOMOTIVES commemoratives, original sculptures, minted in full-Troy-ounce bars of solid .999 fine silver.



Bars Shown Actual Size.

10 Months of Price Protection, Despite Soaring Silver Prices.

Today, you find less and less offers of new silver bars. That's because the price has risen so sharply. The collector who bought last year is realizing price appreciation this year.

Despite this inflationary trend, The Mount Everest Mint guarantees the price of $12.00 per bar for all ten (10) months in which the subscriber builds his 10-bar set. Subscribe now and you get today's prices through ten tomorrows. That's an inflation hedge!

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You may recall from your school books how important railroads were in the Civil War. The "General," captured by Union Troops and recaptured by Confederate Troops, had one of the most hair raising adventures of the war. And, of course, it was the Baldwin Works' number 325 which drew Abraham Lincoln's funeral cortège from Washington to Illinois for the people to view their slain leader.

American ingenuity showed brilliantly in its railroads. Americans put a "leading truck" on a locomotive to make it climb hills better. They added power and length. Today, a 100-car freight train is common. Railroad freight made many new cities possible. Today, railroad freight may save our cities during an energy shortage.

A framed placard to hold your bars, and a slipcase to hold the placard, will be issued with your third bar (at no extra cost).

Railroad memorabilia ranks high among collectors' items.

Millionaires bid for lanterns from an old caboose. New scale models of century-old trains sell out to generous grandparents (who really want to play with them themselves). Restaurateurs redecorate antique railroad dining cars to serve as restaurant wings.

Railroading is "in" — today.

There will be only *one* silver bar edition of THE GREAT LOCOMOTIVES. It is strictly limited to 5,000 subscribers. To acquire a low serial ownership number on this classic, mail your subscription application early.

Mail to: R
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141 Terwood Road, Willow Grove, Pa. 19090

Please reserve, in my name, a serially numbered Proof set of THE GREAT LOCOMOTIVES, Series One. This set is to consist of ten (10) commemorative silver bars. Each bar will contain one Troy ounce of .999 fine silver. Each bar will be shipped in a mint-sealed card, at the pace of one bar per month. The first bar will be issued later this month.

I agree to prepay for each bar shipped. My remittance for the first month's shipment is enclosed. I understand that with the issuance of the third bar, you will send me (at no extra cost) a framed placard which will house the entire collection of ten silver bars, and a slipcase to hold the framed placard.

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Bullion & Numismatic Coins: an interview with Walter Perschke

Walter Perschke possesses a unique set of credentials that make him an ideal source of information on all types of coin investments of both the numismatic and bullion classification. He is proprietor of NUMISCO, one of the oldest and largest coin dealerships in the United States. He is president of both the National Numismatic Network, Inc., a teletype network for coin dealers, and Aureus Ltd., a unique closed-end investment fund in gold and silver coins. He is an active trading member of the MidAmerica Commodity Exchange and a contributor to the GUIDEBOOK *and* HANDBOOK *of United States Coins. In addition he also assembles and manages investment portfolios in coins and publishes a newsletter.*

Robert H. Meier, REASON's *Special Editor for this issue, asked Perschke about his views on good and bad buys in numismatic and bullion coins. In addition to giving specific tips concerning the advantages of purchasing particular coins, Perschke suggests how the investor can avoid pitfalls posed by unscrupulous dealers, and tells how investors have fared who have bought coins from the government.*

REASON: When investors enter the gold coin market, it seems that they will commonly purchase quantities of both the Mexican 50 peso and the American $20 gold piece. Since these two coins are about the same size but have decidedly different price structures could you please discuss their relative merits for the investor?

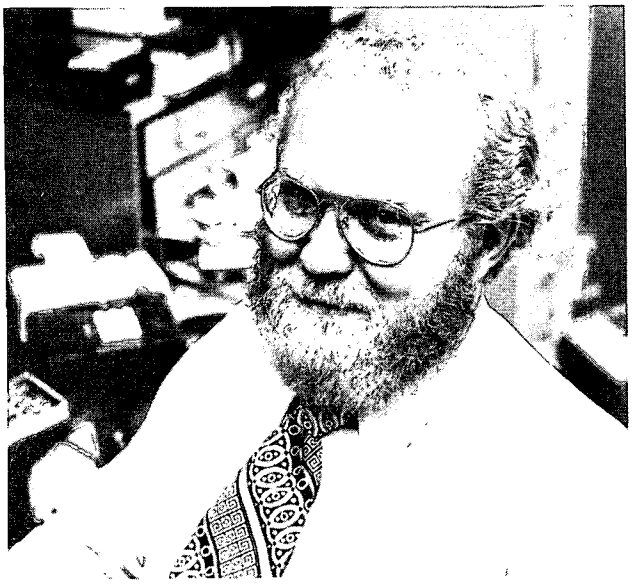
PERSCHKE: The 50 peso represents the best bullion buy for your investment dollar today. That was not always the case, for there was a time last year when the $20 gold piece sold for less than the 50 peso. Today that situation has reversed and it does not appear that relationship will change. If anything, I expect to see the $20 gold piece continue to go higher in relation to the 50 peso coin. Nonetheless for the maximum bullion hedge the 50 peso is the safest investment an American can make in gold coins today.

REASON: When an investor decides to buy the $20 gold piece he has the problem of which type to buy, namely, either a St. Gaudens or a Liberty. What do you consider to be the better buy in the common date coins?

PERSCHKE: The situation changes from time to time, but at present the St. Gaudens is a much better buy for the money because most of the Liberties represented on the market today as uncirculated are actually circulated coins. During the monetary crisis in May 1973, circulated $20's sold at a $40 discount to the uncirculated ones. Today that discount is approximately $10. For this reason the investor should stick with the St. Gaudens as most of these are not circulated, helping minimize the chance that they would unknowingly buy circulated as uncirculated coins.

REASON: It seems that the $10 Liberty is a coin that might be neglected in the rush for the $20 gold piece. What are your personal feelings about this coin and some of the special advantages it might have?

PERSCHKE: At the present time you can purchase two $10 Liberties for less than the price of one $20 Liberty. With that parity situation I think it is definitely advisable for the investor to turn to the $10 coin. I would only advise this, however, for the longer term portfolios, say, three years or longer. Eventually the $20 coin is going to price itself out of the average income market and will be ultimately replaced by the $10 Liberty. But you may have a



situation where the spread between the circulated $10 and the circulated $20 temporarily changes against you and becomes even wider in the short run. Consequently, this type of investment should not be made for the short term, like six months or a year.

REASON: The British sovereign is perhaps the best known gold coin in the world. How do you feel about the coin for investment purposes?

PERSCHKE: The sovereign still maintains a substantial premium over its melting weight. Today's price is approximately $216 per ounce of gold. The Mexican 50 peso, which is today the best bullion buy, can be purchased for $177 per ounce, these figures being based on a gold price of $150 per ounce. You can see the premium on the 50 peso is much smaller than on the sovereign. Bear in mind that there is no shortage of either sovereigns or 50 pesos. The premium on the sovereigns has varied in a wide range from 11 percent to as high as 65 percent over its melting weight and I don't feel as safe putting an investor into sovereigns as I would into either U.S. gold or the Mexican 50 peso.

REASON: Can you think of any lesser known gold coins that might be good buys for the investor?

PERSCHKE: Although coins of this type have their advantages, they share one common detriment in that they are not as marketable as the Mexican or U.S. coins. The Turkish 100 piastres is an excellent bullion buy but the re-sale market is soft. The Russian 5 ruble was at one point the lowest premium gold coin available, but this is no longer the case. The 5 ruble is popular because it is small and could be readily used in barter if necessary. The Swiss 20 franc, the Italian 20 lira, and the German 20 mark were all formerly low premium coins which are no longer in this bracket. Nevertheless, they represent excellent long term buys but they should be considered as numismatic gold. The French 20 franc has been, and is being restruck by the French government; consequently, I would not consider adding this to a normal portfolio at this time. The Netherlands 20 guilder is similar in that it is also being restruck along with the Netherlands 1 ducat and these two should only be considered as low premium gold. The Columbian 5 peso has closely followed the price of the sovereign. We advised our investors some months ago to trade their 5 pesos for Mexican 50 pesos. The premium on the 5 peso, like the premium on the sovereign, has subsequently come down. At the time of the recommended trade, people were able to increase their actual bullion holdings by 40 percent without any additional cash, simply by trading the 5 pesos into the lower premiumed Mexican 50 pesos.

The only other coin that occurs to me is the Hungarian 20 korona. I consider this to be an excellent long term buy. It has not been a very popular coin and is not heavily promoted. The 20 korona is not likely to be restruck and consequently affords both a numismatic and a low premium bullion hedge. Most of these coins in varying portions should be included in a larger portfolio.

REASON: Since the Treasury is now allowing the importation of the Austrian 100 corona restrike we are seeing it take some of the limelight from the Mexican 50 peso as the coin commonly purchased for a bullion position. How do you rate these two coins that seem to perform similar functions?

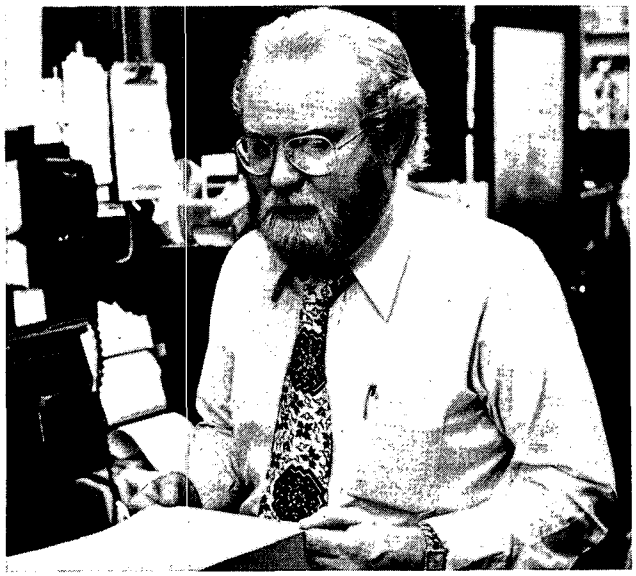
"The Mexican 50 peso represents the best bullion buy for your investment dollar today."

PERSCHKE: Right at the present time the Mexican 50 peso is still the better bullion buy. If the Austrian restrikes are the cheapest gold available to the U.S. citizen by a function of 10 percent under the 50 peso, then he might consider putting them in his portfolio. But, for instance, if the premium on the Mexican 50 peso is 25 percent and the premium on the 100 corona is 22 percent, for the 3 percent difference the investor should definitely purchase the Mexican coin. First of all they are more marketable; secondly, they have at least some potential numismatic value.

REASON: When one considers making an investment in numismatic coins as opposed to bullion coins there is always the question of how well numismatic premiums would hold up if we were to get a serious recession and/or depression.

PERSCHKE: First of all I don't think we are going to have *all* the symptoms of a recession. We may very well have an inflation coupled with a recession. Therefore, I feel the numismatic coins cannot only be related to a recession or a depression but must be considered in the light of an ongoing inflation. Numismatics provide the holder with a far better inflation hedge than anything else I have ever seen. In addition, the market for these coins is broadly based. Quite obviously the longer the recession, the less the numismatic premiums will hold up. Nonetheless, I feel there is no finer inflationary hedge than numismatic gold and silver coins. If we change the scenario and begin talking about a depression then we have a different situation. There is no question that numismatic coins are not a satisfactory depression hedge; for that we have to start dealing more with low premium coins, not silver, but gold coins. Silver is very much tied to the world economy and its price will never hold up in a classic depression.

REASON: Some people feel that the time is already at hand to begin converting their numismatic holdings to a bullion portfolio. I would guess that you feel that this is not the time for that market strategy, but I would appreciate some further comments.



PERSCHKE: I think the decision to convert from numismatic to bullion type coins is premature. I don't think we can satisfactorily assume that we are not going to have the inflation that numismatics will protect you against. For instance, we have done our own in-house projections that are talking about food costs being 60 percent higher between a year and 18 months from now. That is certainly a very substantial inflation, and numismatics will do a far better job of protecting you against that inflation than low premium gold or silver coins. In the period of time that gold rose from $35 per ounce to its present level of $150 the numismatic gold coins outperformed the lower premium bullion coins. In addition, during the long period of time that gold was fixed at $35 the numismatic gold coins had appreciations of between 15 and 20 percent a year.

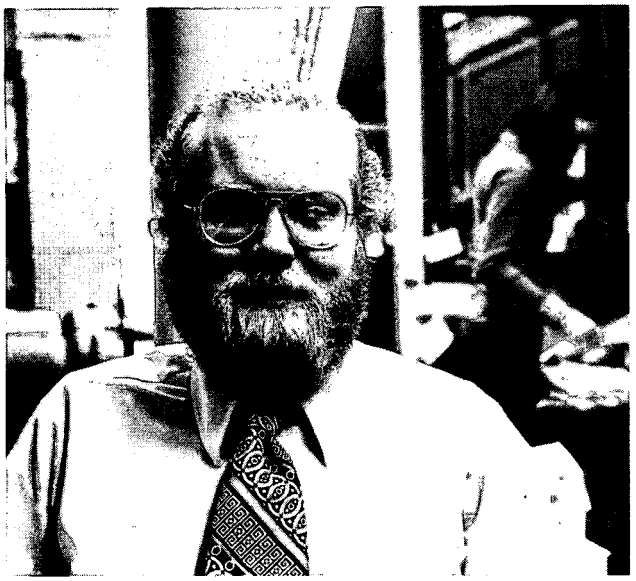
REASON: It would seem very important to understand the grading of coins if an investor decides to enter the numismatic market. I understand that there is more than one grading system and that subleties are very important. Perhaps you could explain some of the ramifications of coin grades vis-a-vis the price of the same coin in a different grade.

"Numismatic coins provide the holder with a far better inflation hedge than anything else today."

PERSCHKE: There is no question that grading is vital and that the investor's best protection is his own expertise. However, this can be acquired from a competent dealer who is willing to take time to show the difference in grades visually. We have on occasion sold an investor a complete set of common gold or silver coins in every grade so that he would have them for benchmark purposes. The major distinction of concern is the difference between circulated and uncirculated. For example, in 1970 the type II one dollar gold coin in extremely fine circulated condition sold for approximately $200. The same coin in uncirculated condition sold for $500. Today the circulated coin is worth approximately $450, and the uncirculated one, $3,000. However, these two grades can appear very similar to the novice investor. In addition, there are people who are "processing" or "whizzing" coins to give them a sheen so that they have the appearance of being uncirculated. Needless to say they are unscrupulous and prey on people who are new to numismatic investing. The most substantial protection you have after personal knowledge is to patronize a reputable dealer who has been in business at least five years and who knows, and is willing to explain, all these factors to you.

REASON: Counterfeiting is another problem which has scared some people from coin investments. Just how big a problem is this to the industry and the investor?

PERSCHKE: I believe that counterfeiting is a grossly overrated problem. It is a problem, but nowhere near what the uninformed press would have you believe. People frequently ask, "Well, how can I be sure these Mexican 50 pesos are real?" The answer is simply a matter of economics. It would not pay any counterfeiter to counterfeit a 50 peso or any other low



premium gold coin, any more than it would to counterfeit one dollar bills. In numismatics the problem is more difficult to define but the technological requirements for minting are such that it prevents the market from being flooded with any thing approaching quality fakes.

REASON: How about foreign numismatics?

PERSCHKE: The risk you run with foreign numismatics is that many foreign governments have shown no reluctance whatsoever to restrike their own rarities. Consequently, the investor is in some jeopardy that his rare coin will be restruck by the government that officially issued it.

"Silver is very much tied to the world economy and its price will never hold up in a classic depression."

REASON: What do you consider to be the ideal commitment for the beginning numismatic investor?

PERSCHKE: The basic numismatic investment any investor should make is a U.S. type set. This is one of each of the 12 different gold coins minted in this century. This would include three one dollar coins, a $3 coin, two 2½'s, two 5's, two 10's and two $20 dollar gold coins. Beyond that, I think I would start date sets of the U.S. $10 Liberty and both gold pieces (St. Gaudens - Liberty). In addition, I would begin buying some common date $5 gold pieces in both the Indian and Liberty series. And finally, I would recommend the purchase of common date $10 Indians, preferably in uncirculated condition.

However, an interesting combination of numismatic and intrinsic values would be to assemble a date set of Mexican 50 peso coins from 1921 through 1931 inclusive. There are several other excellent investments in foreign numismatics, unfortunately, market availability of most of these coins would preclude me from mentioning them in this interview. It must also be remembered that in a crisis situation the market for these coins could simply disappear.

REASON: How are the people faring that have been buying coins from the government over the years?

PERSCHKE: Generally people who have purchased coins from the government's special issues over the years have lost money on their investments. These coins and coin sets normally sell at a discount in the after market and it is many years before the initial purchase price can be recovered. There are a few notable exceptions, the 1970 mint and proof sets are selling at a premium to their issue price and a few of the silver dollars which the government issued in the special sales are selling at a premium, but part of this can be attributed to the enormous rise in the price of silver. The Carson City series of silver dollars with a few exceptions are all selling at a discount to the issue price of $30 per coin. The exceptions would be the 1890 and 1891 Carson City coins, which are currently selling at about their open market minimum bid price.

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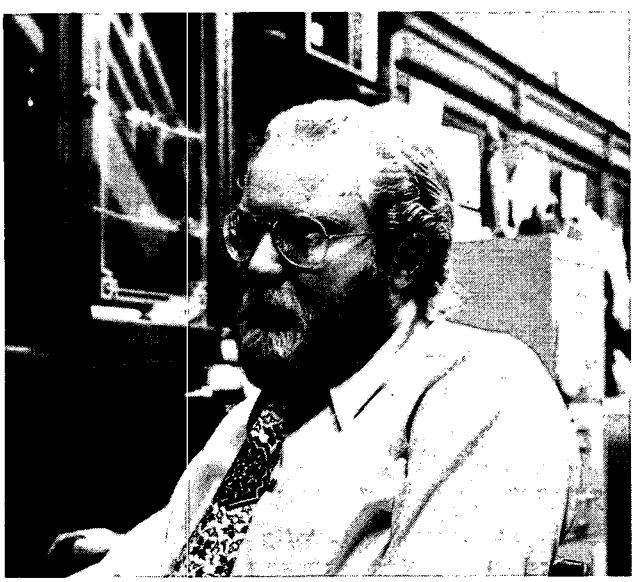
REASON: Do you have any further suggestions for silver numismatic investments?

PERSCHKE: Well, the quality issues, the scarce issues, not necessarily the most expensive ones will over any long period of time, say 5 years or more, always show a nice appreciation and by that I mean 20 to 40 percent a year. Particular suggestions would be uncirculated silver dollars, uncirculated walking Liberty halves, uncirculated Mercury dimes and the early uncirculated Washington quarters. In the Washington quarters I am speaking of the 1949 and earlier dates.

REASON: How about proof sets?

PERSCHKE: Proof sets should be looked at as not necessarily a long range investment but should be bought in periods of price depression and sold when everybody else wants them. The early proof sets (1950 and prior) probably represent the best long-term hedge. The late proof sets (1957 to 1964) will benefit from the rise in the price of silver and represent a combination of some numismatic and intrinsic value. I personally do not recommend proof sets for long-term appreciation. They have proven to be an extremely conservative investment and not as productive as other alternatives.



REASON: The silver bar market has experienced tremendous growth in the last several years but the whole market has that "Tulipomania" quality about it. Would you care to comment?

PERSCHKE: Possibly the only difference between Tulipomania and the silver bar market is that silver bars do have *some* intrinsic value. It has been their only saving grace in the last six months. Bars with premiums as high as $150 are now selling for $20 to $30 per one ounce bar. We advised people to get out of the high premium bars as long as nine months ago. Now the lower premium bars have risen in price but the rise is completely attributable to the increase in the silver's price. When silver was $2 per ounce these bars sold for $4 an ounce. Now these bars sell for $5.50 an ounce but silver also sells for $5.50 an ounce. So while a bar owner has realized a 35 or 40 percent appreciation on his money, if he had had the same money invested in silver coins he would have realized an appreciation of 275 percent. The gimmick used in selling these bars is the limited edition concept. In most cases the edition is only limited by the number of people that are willing to buy it. After all, if there are only 10 bars of one type and you have only 9 buyers you have a glut on the market. The limited edition craze has reached its logical extension in the fact that now even pot and pan companies are issuing limited editions of their wares.

If you wish to purchase silver plates and other commemorative pieces produced by various private mints, you should do so because their artistic merit appeals to you; not because you rationalize them as a high intrinsic value investment.

"We have done our own in-house projections that are talking about food costs being 60 percent higher between a year and 18 months from now."

REASON: Although the collecting of ancient coins might seem a bit esoteric to some people I would be interested in hearing your opinion on this investment area, also.

PERSCHKE: This market for many years lay essentially dormant. The supply situation was substantial, the demand was very small. In the last three years I would say this has reversed, particularly with the gold and silver issues. For instance, a high quality Roman Aureus four years ago sold for $1,200 to $1,500; today the same coin would be priced at between 8 to $12,000 and most of this increase has been within the last 18 months. The silver coins have not experienced such a spectacular rise in price, but nonetheless they have also represented an excellent numismatic investment, and to a lesser extent the high quality copper coins also. The difficulty here is getting into the market. The expertise required is substantial; again there are counterfeits of the more expensive coins and in many cases they are not as easy to distinguish and in many cases were made 700 or 800 years ago. However, an investment company with the properly qualified personnel can provide you with the expertise necessary for buying these coins. ◧

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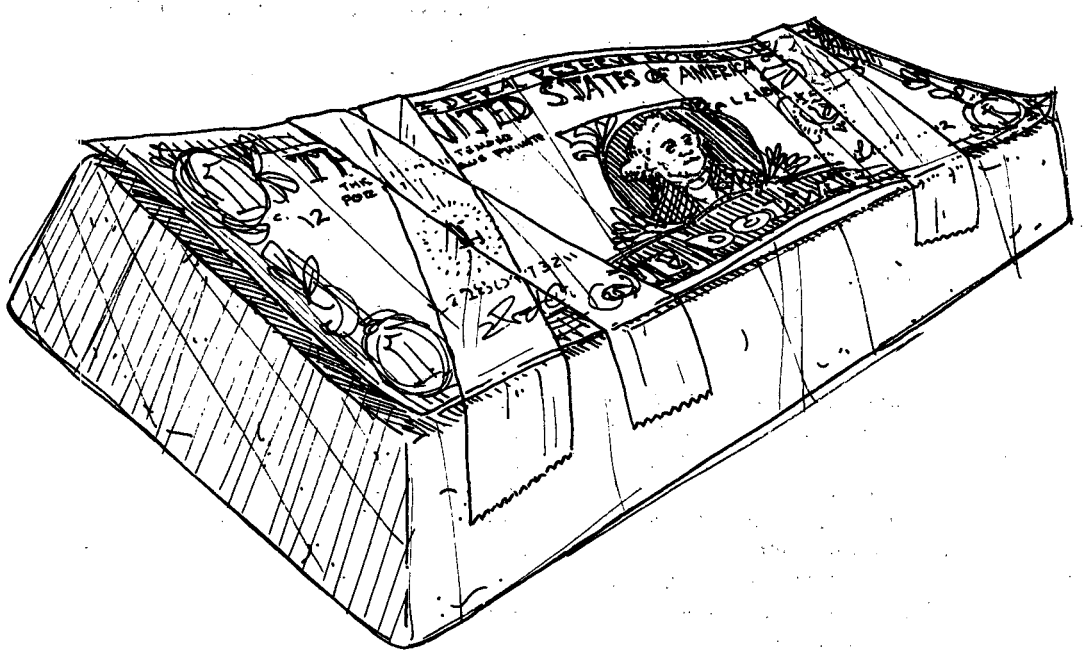

The Federal Reserve Vs. Sound Money

Alden Rice Wells

Alden Rice Wells is the editor and publisher of the ALDEN R. WELLS MONETARY REPORT, *an investment advisory newsletter, and the* ALDEN R. WELLS QUARTERLY, *a general review of society with emphasis on money and taxes. Mr. Wells presented the text of this article to the 1974 Monetary Symposium, sponsored by the National Committee to Legalize Gold, in New Orleans in January.*

When the fabric of society is torn, as it is today, wise men do not shout "Chaos" just as they do not shout "Fire" in a crowded auditorium. At such times they remain cool. They recognize that those in charge have become confused by poor judgment and serious mistakes. We here today have increased our own capital while others were losing theirs and earned the respect of our fellows because we correctly anticipated these present disorders. If we are to continue as useful members of society we cannot say "I told you so" nor shout "The Russians are coming." America is big enough to correct itself. Let us help.

Why does our government declare it illegal for us to own gold? Is it not because Congress steadily abdicated its functions in favor of the President until in recent years he became sovereign? He alone engages us in wars. Control of money was given by Congress to the Federal Reserve, a bureaucracy held in fief by the sovereign. Constitutionally both war making powers and the regulation of money are Congressional functions. When power is so centralized, it is fought over by power hungry men. From such conflicts emerge men unfit to govern. Instead they steadily restrict our freedoms so that they can rule without restraint. The freedom to own gold is among the first to be lost.

But I am encouraged. Congress is now trying to recover its authority. A mild limit on the President's power to wage war was passed over his

veto. The "emergency" Gold Act of 1934 was lifted by Congress. It still did not have the authority necessary to take the decision away from the President, but I think it will in time. These are signs that the people learn even without leadership. They learn, not from their elected leaders, but from teachers such as "The National Committee to Legalize Gold." Mr. Blanchard and his Committee should be congratulated because they have gone to the heart of one of the two major problems disrupting our country. I must now move on to that lugubrious word:

ECONOMISTS

For the first century and a half the people of this country were interested, sometimes passionately interested, in how their money was created, circulated, and who benefited. Since World War II this interest has evaporated. Discussion surrounds consequences, not causes. Inflation and controls stir passions today. Yet inflation is the result of the depreciation of money. Why do not the people insist, as they did in the past, that they be told how money is depreciated so that it can be corrected? The answer, I believe, is that we have created since World War II a new class in society called economists who are really educated fools. Except for a handful, most of whom are here, they are dull, uninquiring of mind, have no desire to learn the truth, and abandoned common sense when they received their diplomas. So today the public is misled into believing that the result is the cause. For economists to be as effective in misleading the public, as they have been, they had to have a powerful arm of government backing them. This was found in our Federal Reserve System with its own interests shared by economists. When ownership of gold was first forbidden the Fed was spending about $25 million annually of our taxes. Today it spends almost $500 million. Its staff has proliferated tremendously; its senior officials have repeatedly insisted that they control our money and would lose control if we are permitted to own gold. Economists who, without question, accept their word find a home in the Fed. When, at last, in the Kennedy Administration the Fed captured the Treasury with such men as Roosa, the Fed and the profession of economics became as powerful as the Pentagon. Why would they admit that they had been continuously wrong, and thus miss out on a good thing? Objective evidence of inflation, high interest rates, and two devaluations did not convert them because long ago bureaucratic necessities replaced the good of the country. When stating a minority opinion, as I am accustomed to do, I must, unlike those who swim along with the majority opinion, prove to be true to what I have said. So let us examine that institution a little closer.

THE MIRACULOUS FEDERAL RESERVE

Beginning in 1958, 1959, and 1960 our sales of gold became such a flood that our gold reserves sank to $17,954 million from a previous high of $25 billion. When, in a brief period of time, $7 billion of gold is bought by foreigners at $35 per ounce any rational person would conclude that we were selling it too cheap. Not so the Kennedy Administration. Influenced by Mr. Roosa, who was moved from the New York Fed to the position now occupied by Mr. Volcker, it was decided to keep the price at $35 by force. As was to be customary for all matters in succeeding years, no attention was paid to the fact that our gold was a finite sum. How did it end? After $4.5 billion more had been sold, by the fall of 1967 the Pentagon became alarmed. It insisted that a floor of $10 billion be set to protect our wartime necessities. In the next six months $3.4 billion was sold. At precisely the $10 billion balance, on March 18, 1968, sales were stopped. After 60 percent of our gold had been sold at $35 per ounce, the average American would assume those responsible would be discredited and the economics profession

"When the Federal Reserve began stating in louder and louder terms that it could create money at will, economists believed it."

institute an inquiry. Instead both drew a curtain between the public and the truth. That curtain read "A great advance in money management. We are succeeding in demonetizing gold."

In 1961 Mr. Roosa also pushed for "swaps" to be run by the Fed. Congress was ignored. Mr. Kennedy, Attorney General, gave Mr. Kennedy, President, the legal opinion that he had the right to authorize them. When Mr. Roosa publicly announced them and stated that this innovation was a great advance, because the Fed had much more power in this field, I wrote a reply and sent a copy to Alfred Hayes, president of the New York Fed. My reply made quite clear that the Fed had no power at all in this field because the Treasury owned the gold necessary for ultimate settlement, and the Fed could act only as agent for the Treasury. Mr. Hayes was very angry. In fact an old friend of mine, George Ellis, then president of the Boston Fed now head of Keystone Funds, told me that the whole top echelon of the Fed was furious. That didn't mean they were learning. Even after a number of trips to the Treasury to obtain $100 or $200 million of gold for settlement, they still did not learn.

Beginning in May 1971, the Fed started selling huge quantities of foreign currencies in the forward market without making provisions for "swap" cover. When the time came in August to deliver the currencies it had sold, it had no plans. The Treasury was too near the $10 billion floor set by the

Pentagon to help out, yet over half of the $3 billion short position was due New York banks, who in turn owed it to their customers. Surely only fools or economists could have gotten themselves into that position. What did the Fed do? Like "go-go boys" caught in a similar bind, it resorted to fraud with a coverup. Over $1.0 billion foreign currencies were borrowed from the Swiss Bank, the B.I.S., and the Belgian Central Bank on Wednesday and Thursday, and on Friday $750 million from the Bank of England. On Saturday the fraudulent default came. With it went the Bretton Woods agreement that for a quarter of a century had been the cornerstone of economic cooperation with our allies. The cover story was wage and price controls. Not only the press, as you might expect, was deceived by the cover story, but also the economics profession which, at least, should have sought to find out what happened. Congress slept as soundly as ever. The cover story had worked. Only our allies, who had been betrayed, were angry, but they don't vote in our elections. Gold became increasingly dear as more people learned that a government issuing only paper money cannot be trusted.

"The Fed has made a profit since its beginning of $65,192 million from the demand by the public for more and more paper currency."

The increasing centralization of government produces a corresponding dependence among those whose freedom means little to them. Among these are economists. When the Federal Reserve began stating in louder and louder terms that it could create money at will, economists believed it. They ignored basic accounting rules or even the common sense that clearly denies that any person or institution can create something out of nothing.

The Fed claims that it can buy or sell any amount of Treasury securities it wishes. It claims it does this by crediting member banks' reserves (a deposit by banks in the Fed). Once a week the Fed issues a balance sheet that is reported in the press and is available free for the asking. Do economists look at it? No! If they did, they might see that, from the one I have in hand, Treasury securities totaled $76,565 million but member bank reserves were only $28,378 million. Where did the $48 million discrepancy arise? Or if they wish to look in the *FEDERAL RESERVE BULLETIN* they would discover that on December 31, 1941 the Federal Reserve owned only $2,219 million Treasuries but member bank reserves were $12,812 million. A little arithmetic would reveal that Treasuries rose $74,346 million during a period when member bank reserves rose only $13,568 million. Surely some economist should have asked where over $60 billion Treasuries came from that are not accounted for in the Fed's explanation. Surely there must be some economists who know that assets and liabilities must equal each other. But none, but the few here, in or out of the government raised such questions.

They did not even ask why Morgan Guaranty would sell $25 million Treasuries to the Fed for a noninterest bearing deposit in the Fed. Yet obviously when the bank did, it had in mind reducing that deposit by a like amount and buying other Treasuries or loaning to U.S. Steel. The record shows that all government bond dealers accredited to the Fed did just that. How then did the Fed balance its books? What effect did these transactions have on the money supply if the dealers were merely substituting one government security for another or loaning to a company rather than Uncle Sam? How could deposits rise and thus reserve requirements? You will not find an answer to any of these questions in universities or the books published by the Fed. So I must supply answers if we are to see how our money system really works.

FIRST: CURRENCY

Ninety percent of the Fed's income comes from interest on its Treasury securities—interest paid by the taxpayer. Out of this total of about $3.5 billion the Board of Governors allotted itself $43 million for the year ending December 31, 1970. Of this $22 million went to the Bureau of Printing and Engraving for new Federal Reserve notes and to the Federal Reserve agents in each bank to keep a record of them and destroy those no longer fit for circulation. Consequently new notes arrived in the Federal Reserve agents' hands without cost. The Federal Reserve banks themselves acquire these notes without cost by delivering worn out notes or providing the agent with the serial numbers of Treasuries they had acquired. Formerly, they could also acquire these notes by specifying the gold certificate numbers they owned, and before that, gold. The Federal Reserve sells this currency on demand to member banks at face value thus profiting by 100 percent. Out of this 100 percent profit it buys equivalent Treasury securities to satisfy the Federal Reserve agents. On the weekly balance sheet I showed you earlier, the Federal Reserve Agents' Accounts show $65,192 million Federal Reserve notes outstanding of which collateral was $64,530 million Treasury securities and a small balance of gold certificates. The Treasuries pledged with the Federal Reserve agents were 86 percent of all Treasuries owned by the Fed that week.

Shall I draw the clear conclusion that the Fed has made a profit since its beginning of $65,192 million from the demand by the public for more and more paper currency? Shall I also draw the clear conclusion that the discrepancy between the Treasuries owned, and member bank reserves, has been

"Limitless circulation of gold coins (would be) the most potent stabilizing force yet devised."

accounted for? Finally the retention by the Fed of all this profit and its investment in Treasury securities creates an inflation of like amount. What sense does Dr. Burns make in demanding in 1973 price and wage controls when his own organization depreciated money in 1973 by over $5 billion?

NOW: GOLD

Before 1934 the Federal Reserve owned all our monetary gold. When it bought gold, it paid for it; when gold was sold, it received the proceeds. The amount of Treasury securities held rose or fell by the same amount—thus creating instability in the money markets. President Roosevelt transferred ownership of this gold to the Treasury to avoid arguments with the Board of Governors over purchases of gold to get the price up. However he did not want the Treasury to pay for these purchases as he was already being severely criticized for a large budget deficit. Consequently gold certificates were given to the Fed for the amount of gold received, and more with each purchase. As the Fed accumulated more certificates, it credited the Treasury with a deposit for a like amount, and the Treasury paid for the gold. Thus the reported Treasury deficit would be less, and the Treasuries held by the Fed would decline as it was forced to sell to honor the Treasury's withdrawals. That is why the Fed had only a little over $2 billion Treasuries in 1941 and this process became a major factor in prolonging the depression seven years. Eighteen billion dollars of gold purchases were handled that way. For the 11 years ending March 18, 1968, the process was reversed. Fifteen billion dollars of gold was sold. The proceeds were given to the Federal reserve who invested them in Treasuries and with the multiplying factor caused inflation, or rather depreciation of our money by $100 billion or more.

I believe I have now proven my minority opinion that the inflation we have suffered has been the result of the depreciation of money by the government, and that this has been allowed to happen because the economic profession consists of educated fools.

THE CURE

Since it is hopeless to believe that the executive branch, or the Federal Reserve, or economists can work out a cure for this situation until we run into a major depression (if then), I will attempt to outline it now.

Paper currency is an easy matter. Only the Treasury should issue it, sell it to the Fed at face value, and use the profits to retire debt. This can be short cut further by the Fed delivering the Treasuries it purchases out of its currency profit to the Federal Reserve agents to be destroyed along with the used Federal Reserve notes. Only a small amount of presently held Treasuries need be kept in a suspense account for seasonal fluctuations. No further inflation would arise from this source, or deflation as happened in 1949 and the mid-1930's, when the public uses less currency.

The gold problem is somewhat more complex. The objective should be a limitless circulation of gold coins of two denominations. One should contain one ounce and the other one-half ounce of pure gold. When inflation occurs because government expenses are too heavy or banks are financing the deficit, the public will acquire more gold coins. This in turn reduces bank deposits, which reduces bank credit, which in time brings the government and bankers back to their senses. The process also works in reverse. Consequently it is the most potent stabilizing force yet devised. It justifies "The National Committee to Legalize Gold" as the single most useful committee in America.

But a limitless circulation of gold coins against a finite amount of gold means that price must take up the difference between supply and demand. The first decision must be, therefore, that the coins

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cannot have legal tender value. Most of our money is not legal tender because 95 percent of money payments made today are by checks that are not legal tender. The usefulness of legal tender is chiefly to provide a legal basis for action against counterfeiters. No legal tender—then no face value. However, since the gold coins will be used as money, there should be no tax on profits nor credit on losses. A further refinement is that all institutions—the Treasury, the Fed, banks, etc., account for their transactions on a Last-In-First-Out not a First-In-First-Out basis. Individuals need not account for their transactions.

With this clearing away of several problems we can proceed on how gold coins can be put into circulation without disturbance to the monetary system. The disorders in the world that have already pushed the price of gold higher will increase the price if the government announces not only that Americans can own gold but the government will mint gold coins. At $200 per ounce the Treasury's gold stock has a market value of about $60 billion. All of this should be converted into coins with, as we mentioned earlier, no stated value but a guaranteed weight.

"If banks are refused the right to borrow money except from other banks . . . then bank credit expansion will not depreciate money."

Of this, $10 billion must be set aside for the Defense Department. Although this is less by weight than previously required, the government can easily get, in an emergency, most of the balance from its own citizens, as we shall show, just as the British government did in World War II. The remaining steps are as follows:

1. The Treasury sells gold coins to the Fed at the daily market price.
2. Commercial banks buy their requirements on the same basis.
3. The public buys from commercial banks at this price.
4. The Treasury, Federal Reserve, and Commercial banks will require some inventory. That is why they must account for it on a LiFo basis.

It is desirable, however, that banks as well as private individuals become aware of the significance of gold as money. Consequently the noninterest bearing and frozen reserves which they must today keep on deposit in the Federal Reserve should be converted into gold coins. The Treasury can sell $28 billion of their $60 billion to the Fed at current prices in exchange for Treasury securities held by the Fed and cancel those securities. Second, the Fed should sell, at the same price, those gold coins to member banks in exchange for canceling their deposits with the Fed. Congress would then require that all banks must keep half of their capital and surplus in gold coins. This approximates the $28 billion member banks already hold. From that point on the Treasury will maintain an inventory, in excess of the Defense Department's requirements, by buying or selling in the open market or with special deals with other governments. Never again will it commit its gold reserves to guarantee another international parity for the dollar. The dollar must float.

If these changes are made, it will end inflation or deflation by the Fed. If banks are refused the right to borrow money except from other banks, and also are careful about lending money to the Treasury, then bank credit expansion will not depreciate money. How to keep government spending to reasonable levels is a different and even more complex subject that is beyond this analysis.

No doubt the times will get worse before they get better, but this is the period in which your weight can be felt, as the previous generation's was not during the continuing Roosevelt depression. May I also point out that the Roosevelt solution of a World War is no longer available to us today?

If you wish to avoid a depression, then paper currency, gold, bank credit, and government spending must all be subjected to rational analysis and correction. Since economists, the Federal Reserve, and the Treasury are all opposed to this, then our unfortunate fellow citizens can only hope that we get a competent Secretary of the Treasury before too long.

The cheerful element in this sad story, as I mentioned earlier, is that those who take the trouble to understand money can continue to increase their capital as they watch the government continue to create disorder. ◻

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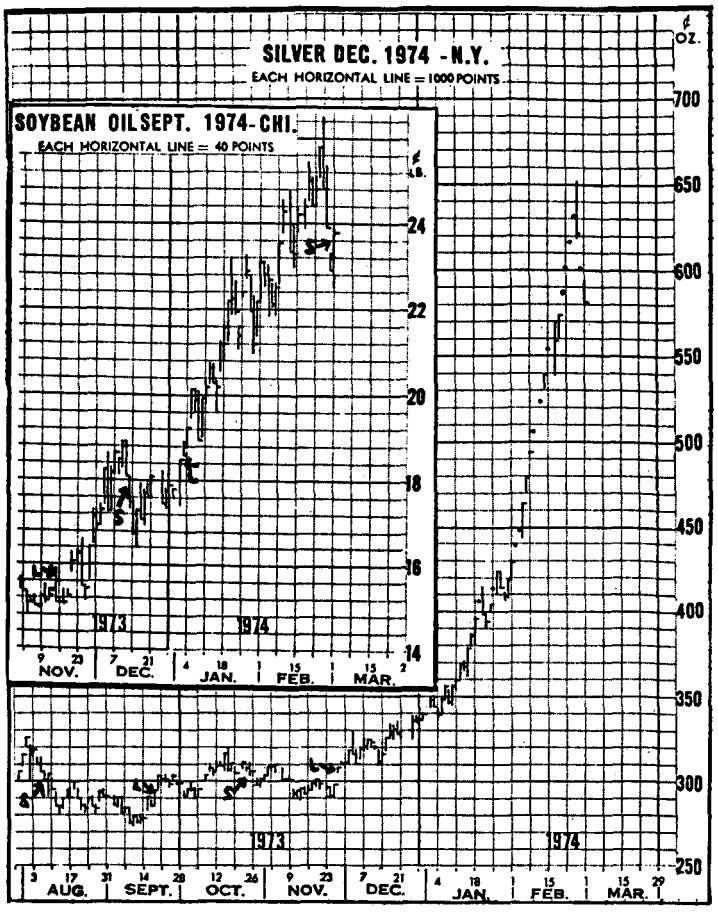

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What You Should Know About Fiscal & Monetary Policy

J. M. Cobb

Most investors understand that their gains and losses are determined (somehow) by government monetary and fiscal policies. The upturns and downturns in the market, or in the economy as a whole, are believed to be significantly influenced by loose or tight money, government spending, interest rates, and other factors which are under the control of the President or the Federal Reserve System. These are respectively the two high authorities which control fiscal policy and monetary policy. Since attempts to manage the economy by means of such policies have proven so unreliable in the past, this article will attempt to provide an overview from which the reader may start in order to formulate his own predictions about the economy.

Fiscal policy is formed initially by the Office of Management and Budget in Washington, directed by Roy Ash this year. With the formulation of the President's budget, the fiscal policy proposals are introduced in Congress. Fiscal policy may involve new taxes, or tax cuts, and government spending. After Congress authorizes a program, and appropriates money for the program (two separate steps), the policy—which by this time is plural—fiscal policies (also known as "pork barrel" legislation) are turned over to the bureaucrats for spending.

ENTER THE FED

Monetary policy is formed by the Federal Reserve Board in Washington. The Board of Governors of the Federal Reserve System are appointed by the President for fourteen year terms. The current Chairman of the Federal Reserve Board is Arthur F. Burns, formerly a professor of economics with a reputation for business cycle research. The terms of the members of the Board are staggered, so that a President will be able to appoint a majority of the Board only if he serves for two terms—and no President can appoint the entire Board. To the extent that monetary policy controls the upswings and downturns in the business cycle, each President must live with and suffer the blame for the monetary policy which the appointees of his predecessor decide upon. In theory the Fed is supposed to be above politics; in fact its policies have significantly moved the government in political directions (witness the Great Depression, and the changes in the role of government which that has led to).

Monetary policy is then executed by the Federal Open Market Committee, which buys and sells securities (usually in the New York market) and thereby makes changes in the money supply. When the Federal Reserve Bank of New York sells a government bond, it collects money; when it buys a bond, it disburses money. In our monetary system, money inside the Fed simply doesn't exist—it is

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created or destroyed as it is issued or collected. The money supply thus grows or shrinks, usually by a factor of 6 or 7 because each member bank can use the notes of the Federal Reserve Banks for fractional reserves.

Many people also believe that the Federal Reserve Board can influence fiscal policy by controlling interest rates. If the Fed can predict the demand for money, and control the supply of money, it can peg the rate of interest and thereby induce the private sector to spend or hold more money. The discount rate is often mistaken to be this "rate of interest." This theory is essentially a misleading notion—although it was followed by the Fed for several decades after the Great Depression. The reasons for this theory will become clear during our discussion, below, regarding the quantity theory of money and the autonomous expenditures theory of income.

The fact about economics which makes understanding the system so difficult is the complex interrelationship of the various significant factors. Each of the quickly visible elements of the economic process will lead to less easily seen changes elsewhere in the market, and it is often difficult to estimate

even the relative magnitudes or relative importance of the changes which *are* reported in the newspapers.

Government policies are considered to be important factors affecting the financial community because they are highly visible (except when the policymakers purposely prevaricate) and because unlike private market trends, they are usually more erratic—and hence introduce the destabilizing shocks which cause the business cycles.

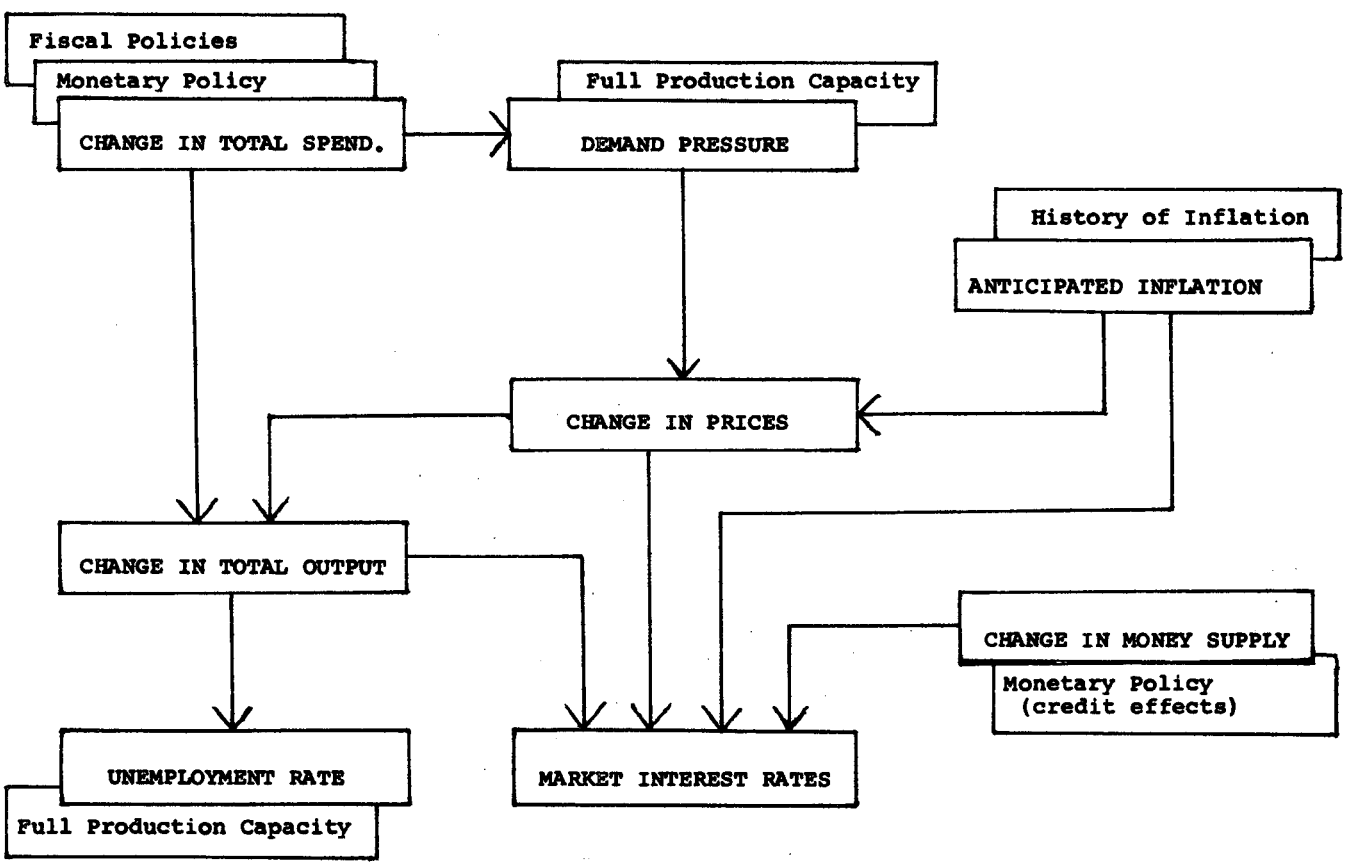

Diagram of a Monetarist Model of the Economy. Only current variables are utilized, except inflation history.

GOVERNMENT'S ROLE

In the past decade, professional opinion among economists has been shifting more and more toward placing primary weight on policy changes by the government as a causal factor for the business cycle, specifically monetary policy, instead of looking upon government policies as a response to strange and unpredictable changes in the tastes of private consumers and investors. The publication in 1963 of an article by Milton Friedman and David Meisleman, entitled "The Relative Stability of Monetary Velocity and the Investment Multiplier in the United States, 1897-1958" marked the turning point, in this writer's opinion.[1] Significantly, two years earlier marked the ascendency in government circles of the so-called "New Economics" of the Kennedy and Johnson Administrations—to which the United States can credit the origins of its present problems with inflation.

The questions which every private citizen wants answered involve the direction of the economy. Private investment plans, not to mention planning for career opportunities or for retirement, all depend upon predicting the future, within broad categories. Individuals who are concerned with the financial markets on a daily basis are even more concerned with predicting the future as accurately as possible. One development in popular economic thinking is the fact that the soothsayers who rely on the monetarist models of the economy have a better track record than the prophets of the fiscalist school. Nothing will sell a theory more rapidly than the accuracy of its predictions—contrasted with errors on the part of competing theories. This has been the recent experience of monetary policy studies, compared with a less impressive record for fiscal policy analysts.

Yet, fiscal policy measures are popular and powerful factors in the American economy. More than a third of total spending is conducted within the government sector. Further, a government deficit which may be financed by selling bonds to the Federal Reserve System will expand the money supply and increase total spending simultaneously through monetary and fiscal policy. In fact, fiscal policy measures which draw funds exclusively from the private capital market will increase total spending to the extent of the government spending, but since private capital is siphoned off, the "multiplier effect" of fiscal policy approaches one for one. This is one reason why fiscal policy enthusiasts focus their attention on Federal government deficit spending and not on local or State government bond issues. Classical Keynesian theory argues that the multiplier effect should be the reciprocal of the average propensity to save (roughly three to one for temporary changes in real income). Economic stagnation is interpreted as the tendency of individuals to hold onto their savings longer than might be "socially desirable."

The creation of new money by the Federal Reserve System, however, does exert a positive and multiplied pressure on total spending because, given fractional reserve banking, one new Federal Reserve Note in a bank vault serves as the basis for loans which in total amount to 6 or 7 times the face value of the cash note. This is the distinction between "high-powered money" and ordinary checkbook money. The important question about a stimulative fiscal policy then becomes: How is the deficit spending to be financed?

"If most people believe a wrong idea, and act on it, then most people will be misled."

Fiscal policy as a theoretical tool became popular during the 1930's because it characterizes the central government in an activist manner "doing something" to create jobs, and generally to put money in the hands of the public to spend. Obviously the government-spending part of the policy was immediately popular with politicians; but the other side of the policy, taxation to pay for government spending, has been much more difficult to manage. The economic theory which assumes that mysterious cosmic forces automatically lead to speed-ups and slow-downs in business activity then looks to an active, counter-cyclical government fiscal policy for stabilization—to run a budget surplus in times of full employment and to run a budget deficit in times of recession. The assumption is that people as a whole sit on large cash balances in times of recession, thereby causing a drop in total spending, and spend themselves into debt in times of full employment, thereby overheating the economy.

In point of fact, the stable factor in these relationships seems to be the amount of real wealth which people desire to hold in the form of cash balances—regardless of boom or bust in the business cycle. When the money supply expands, individuals observe an excess in their real cash balances (adjusted for the rate of inflation) and step up their spending plans. When the money supply stops expanding, or shrinks, individuals tend to slow down their spending plans to keep up their real cash reserves. The business cycle itself can be interpreted as the response of the economic system to the money supply "cycle" which has been managed rather badly by the Federal Reserve and the Treasury.

AUTONOMOUS EXPENDITURES

Behind the support for fiscal policy on the part of economists is the theory that income is determined by the level of autonomous expenditures, which include business investment decisions, home-

building, and government expenditures. These are labeled as "autonomous" because they are not part of a formula dependent upon income, such as consumption and savings are assumed to be. The theory, usually identified with Keynes although it has gone through a number of variations, makes the assumption that there is a "leakage" in the cycle of income, consumption, savings, and investment (Say's law) because savers and those who spend investment funds to purchase labor services and capital goods are different individuals. Sometimes, for mysterious reasons (such as a lack of "business confidence") there is a shortfall in the amount of autonomous investment. In those cases, the theory argues, the government should make up the difference. Direct action by the central government is desired to make up for the lack of will on the part of the individuals in the market. In the 1929-32 period, of course, this "leakage" was the absolute contraction of the money supply caused by the Federal Reserve System. One third of all the money in circulation was removed, and the banking system collapsed.

So now the question becomes: Which theory is correct? The surprising answer is that both theories are *versions* of the same analytical system. Each theory, however, places emphasis on different variables, and each theory makes assumptions about which variables are stable, and which ones are controllable.

Fiscal policy assumes that the year to year ratio of savings and consumption is stable, whereas monetary policy assumes that the demand for real cash balances is stable. The economics profession fell into confusion when it was presented with two alternate theories of the same process, because nobody really knew which variables were more important. Largely on the basis of no evidence at all, the profession adopted the autonomous expenditures theory. The politicians were delighted to go along.

ENTER THE FACTS

In the past 10 years, at last, a significant amount of statistical research has uncovered the fact that the autonomous expenditures theory is less useful in explaining economic events than the quantity theory of money.

> In other words, the simple version of the income-expenditures theory to which we have deliberately restricted ourselves in this paper is *almost completely useless* as a description of stable empirical relationships, as judged by six decades of experience in the United States. Though simple, *this version is substantially the one that is presented in every recent elementary economics textbook as the central element in the theory of income determination.* Such results as we have so far obtained from analyses for other countries strongly confirm results for the United States. On the evidence so far, the stock of money is unquestionably far more critical in interpreting movements in income than is autonomous expenditures. [p. 188, emphasis supplied]

If we can make the assumption that most businessmen and investors have learned their theories of economics from elementary textbooks on the subject, then we can point to an area for profitable investment of time and money. If most people believe a wrong idea, and act on it, then most people will be misled. The books listed at the end of this article for further reading should provide the reader with a comparative advantage in spotting upturns and downturns in the business cycle.

The reader should be warned, however, that we are discussing broad market concepts in a statistical context. The actual decisions which statistics summarize are made by acting individuals, and we cannot predict individual behavior except in very broad average terms. There is a variable lag between a visible movement in the rate of change in the quantity of money and a peak or trough in the market. Here again the more someone would study the relationships, the greater his comparative advantage would become. The monetary policy approach simply has a better track record for success than the fiscal policy approach.

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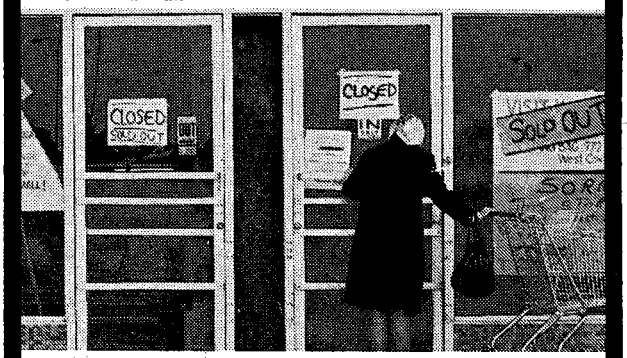

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monetary policy approach, Friedman and Meisleman conclude their article with an important distinction between a widespread belief in the "credit effects" of monetary policy as contrasted to the "quantity theory" approach. The mechanisms of the quantity theory approach have been described above, as they operate through the demand on the part of both households and business for real cash balances. The "credit effects" theory makes the assumption that monetary policy works primarily through the financial markets, affecting the rate of interest, and that the rate of interest then determines the magnitude of autonomous expenditures—which brings us to the same framework as the fiscal policy approach.

The mistake arises from a certain narrow perspective which the financial community automatically assumes. Since "the" rate of interest is important on a day-to-day basis, and since the activity of the Federal Reserve System has a strong effect on the yields of various widely traded securities, the short-term impact of monetary policy in the market will obscure a more accurate analysis of the long-term impact of monetary policy on the economy as a whole. The relevant interest rates which are influenced by a change in the quantity of money are not just those affecting business and the financial markets. The quantity theory of money treats "interest rates" as the abstract category which relates a periodic stream of payments or services to the economic value of the source of these payments or services, and not simply the rate on government bonds or commercial paper (pp. 213-222).

"The real driving force behind the policies of the government is a fear of unemployment."

IMPLICATIONS FOR INVESTORS

In this article we have dealt very generally with the theories which underlie the fiscal policy vs. monetary policy analysis of the economy. There is an accelerating trend among investors and corporate treasurers to pay attention to changes in the money supply. We have not said anything about the motivations for changes in policy. Yet the real driving force behind the policies of the government is a fear of unemployment. Whether it is the spectre of the Great Depression, or some motive to help the poor, or just a prudent awareness that unemployed voters usually vote against the incumbent, Congress and the President are biased in favor of a rapid expansion of the money supply and increased Federal spending (financed by newly printed money, of course).

The attempt to "fight unemployment" by expanding the money supply, however, leads to an increase in demand pressure and to price increases. During the past four years one can see a very interesting pattern in the money supply: it was contracting until the Republicans took a beating in the 1970 elections, followed by a rapid turnaround in time for Nixon's re-election campaign in 1972. Our present inflation is a consequence of the rapid increases in the quantity of money during 1972 and early 1973. In mid-1973 the rate of change fell almost to zero—and now we have reports of growing unemployment, and an increase in Congressional restlessness. Since October (except for the month of January) the money supply has been growing rapidly again.

On the other hand, there is a strong consumer dissatisfaction with the present rate of inflation, and the only way to fight it is to squeeze the money supply. The schizophrenic attempts by the government over the next 10 years to prevent unemployment from rising during election years, and to prevent inflation from reaching levels of 15 and 25 percent (a very real possibility) will produce a series of business cycles which may prove very profitable to the investor who knows what to look for on the financial pages, or who knows which economists and other soothsayers are on the right track. In this brief article, we have only touched on some of the more distinct differences between monetary policy and fiscal policy. The reader will have to go to the primary sources for the really useful knowledge, in order to predict the future according to his own judgment—and to get that confident feeling that he will be right more than half the time. ◻

NOTES AND REFERENCES

[1] The Friedman and Meisleman article appears in Commission on Money and Credit, *STABILIZATION POLICIES* (Englewood Cliffs: Prentice-Hall 1963), pp. 165-268. Subsequent parenthetical page references are to this article.

The reader is directed to the following books for further study:

Milton Friedman, *THE OPTIMUM QUANTITY OF MONEY AND OTHER ESSAYS* (Chicago: Aldine Publishing Co. 1969). For those with a taste for economic theory at the advanced level.

A. James Meigs, *MONEY MATTERS* (New York: Harper & Row 1972). A highly readable discussion of monetarist vs. fiscalist theory, complete with an economic history of the last 10 years.

Beryl W. Sprinkel, *MONEY AND MARKETS, A MONETARIST VIEW* (Homewood: Richard D. Irwin 1971). An excellent "how to do it" book for the investor who wants economics explained to him.

Everyone should immediately write to the Federal Reserve Bank of St. Louis to request placement on the mailing list to receive (free of charge) their weekly "U.S. Financial Data," a compilation of graphs and charts of money supply and interest rates.

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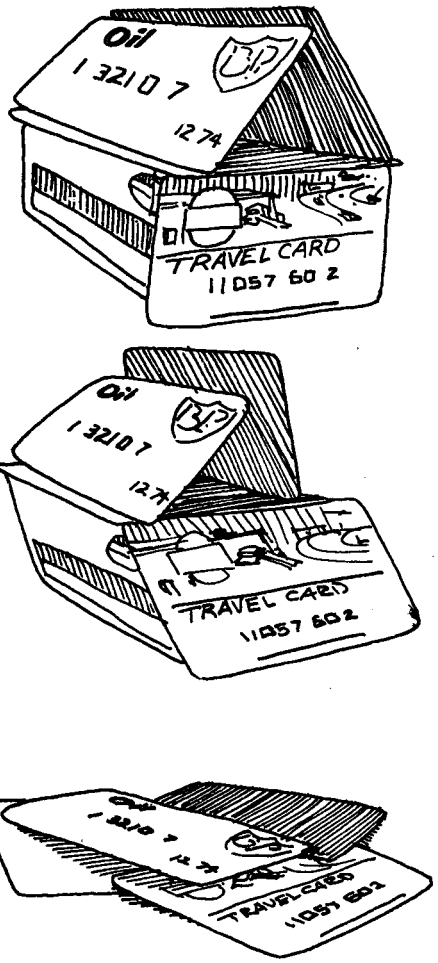

THE COMING CREDIT COLLAPSE

Perry Paris

In recent years, investors and financial markets have been buffeted by a seemingly unending barrage of unprecedented shocks and nearly crippling blows. The demise of an international monetary system, historic levels of inflation and interest rates, soaring food prices and peacetime controls are only a few of the problems. New words are creeping into the financial vocabulary such as credit crunches, floating exchange rates, dirty floats, energy crisis, Phase I, Freeze II and many others. In the land of plenty, shortages abound. In scarcely a decade we have moved from the age of the "New Economists," where the government was confidently expected to fine tune the economy for continuous growth, to one where the credibility of the government has all but disappeared. The world leadership role of the United States has been considerably tarnished. Citizens are even beginning to doubt themselves.

Alexander P. Paris holds a B.A. in economics and an M.B.A. in finance from Michigan State University, and an M.A. in economics from Wayne State University. He is presently an officer of a major institutional investment firm, where he specializes in institutional research. Paris is the author of A COMPLETE GUIDE TO TRADING PROFITS *(Whitmore 1970) and* THE COMING CREDIT COLLAPSE, *to be released later this year by Arlington House.*

A SINGLE CAUSE

Almost all of these seemingly unrelated problems emanate from a single underlying cause. The source of the disturbances is a secular trend of excessive credit creation that has continued unbroken since the 1940's. While the nation's ability to produce real goods and services can only grow at a rate approaching four percent, the creating of credit in all sectors of the economy has compounded at a rate nearly three times as fast. This unhealthy trend has been fostered and perpetuated by the government, with the aid of the Federal Reserve. It was made possible by an entirely new philosophy of government that took roots in the rubble of the depression years of the 1930's. The philosophy was formalized with the Employment Act of 1946 which made growth at any cost a duty of the government and took wings with the ascendency of the New Economists in the early 1960's.

With the government firmly committed to a program of growth and the growing widespread belief that the business cycle was dead by legislative decree, a new reckless overconfidence took hold among corporations, individuals, and the banking system. With this new confidence, the fears that remained from the depression years were gradually forgotten. A new generation arose with a completely changed credit ethic which allowed corporate and personal balance sheets to be stretched thin in the search for maximum growth of earnings for corporations and the good life for the individuals. Even conservative bankers forgot the pains of the 1930's with its bank holidays. The traditional philosophy of adequate liquidity was exchanged for a new banking philosophy of profit maximization and aggressive liability management.

"The growing corporate illiquidity represents a latent deflationary force in the economy that can only be offset by ever larger doses of credit."

To make it all come true the government engaged in the most massive spending campaign in the history of the nation, as large and growing budget deficits became the rule. Much of the spending was

financed by higher taxes at all levels of government. The cost in terms of the loss of personal and economic freedom has been great. The percentage of each dollar of national income that is spent by the government has increased from 11 percent in 1947 to 48 percent in 1972. When politicians failed to acknowledge their deeds by higher taxes, the Federal Reserve obliged by purchasing the government debt and turned it into high-powered money that the banking system eagerly multiplied manyfold into auto loans, mortgages, and corporate debt.

THE DEMISE OF THE BALANCE SHEET

Most of the growth of the postwar years was made possible only by a massive deterioration of the national balance sheets of corporations, banks, individuals and the government. Like good magicians, the Keynesian economists diverted our attention from the balance sheet to the income statement to see the wonder of their deeds. The cost of their rhetoric, however, has been recorded on the balance sheet but few examine it. To understand how this was done, the growth of Keynesian economics must be traced.

"Banks have no choice but to continue to help their clients become more deeply mired in debt in order to keep the system from collapsing."

The determination of many in the 1930's that we must never again allow a repeat of the massive unemployment and hardships of that period gave nourishment to a new brand of economic theory. The emphasis was shifted away from the classical quantity of money orientation toward income and expenditure flows. During the Roosevelt years and the Second World War the precedents for big government were set. Throughout the Eisenhower years the philosophy spread and followers of Keynes waited and planned for their big opportunity. In 1946, as mentioned, the government had been charged with the responsibility of maintaining growth. Finally, in 1961 the New Economists got their big chance and they were ready. It lasted for two presidents.

The theory of the "fiscal drag" was spotlighted. Under this theory, as GNP grows and tax revenues rise, a government surplus grows which, if ignored, could choke off further growth. Therefore, a "fiscal dividend" must be declared in the form of a tax cut or higher expenditures. It did not matter whether more spending was "needed"; new programs would simply have to be invented, for continued growth was the goal. The cult of growth was born. The only trouble was that while politicians leaped at the chance to cut taxes to foil the dreaded fiscal drag, raising them when the "inflationary gap" threatened was a vote of a different color.

"The entire credit ethic that has mushroomed in the postwar years must be changed."

Government spending took on an upward bias. Original Keynesian theory called for deficit spending when the business cycle turned down but surpluses when it was rising. With the fear of fiscal drag and the preoccupation with growth, the disciples of Keynes somehow managed to turn this into a deficit *every* year. They shifted the emphasis from " correcting" the business cycle to propelling growth continuously. The New Economists were no longer content to moderate the economic declines but instead claimed to be able to fine tune the business cycle out of existence. With an attractive and vibrant new president and a willing media that always has a predilection toward activism, the New Economics got off to a resounding start. The New Frontier and then the Great Society programs, with the publicity of early "apparent" success, enraptured the media.

Not surprisingly, the new government attitudes permeated the entire economy. With guaranteed growth and no serious business corrections to be concerned about, growth became the brass ring. Individuals began to borrow more heavily from the future in their quest for the good life in keeping with the goals of the New Frontier. The cult of continuous earnings-per-share growth for corporations began. Those corporations that did not leverage their balance sheets to maximize or maintain steady growth were considered underachievers and pariahs. Growth at any cost did not apply only to the government. Accounting practices were found to be ready sources of the flexibility needed to keep earnings growing. Nor did investors worry that conglomerates were buying growth by destroying their balance sheets. In fact, they did not even examine the balance sheets. Growth was the end that justified the means. Even banks no longer needed the heavy liquid buffers of earlier years. With little chance of serious needs for cash in an economic slowdown, liquid assets became a burden. Growth maximization was also accepted in the conservative ranks of the banks and a new banking philosophy was born.

All through the period, the income statement became the star while the balance sheet was relegated to the wings. The problem is that such trends are self-enforcing and gradually everyone must run faster and faster just to stand still. The seeds of the accelerating world inflation, rising interest rates and volatility of the late 1960's and 1970's, were already being sown. Increasingly larger doses of credit are needed to keep the house of credit cards from falling. Each dose lays the foundation for the following surge of inflation. In short, underlying the long period of postwar prosperity, much of which is becoming increasingly illusory, is a long trend of steadily accelerating deterioration of balance sheets in all sectors of the economy.

CORPORATE LIQUIDITY

It did not take corporations long to contract the growth fever from the enthusiastic government economists and liberal politicians. By the time the New Economists ascended to full power in 1961, the condition of the average corporate balance sheet had already worsened materially in the period following the war. Since 1960, the trend of deterioration has accelerated substantially as the balance sheet was consistently sacrificed to the income statement and continuity of earnings growth.

Illiquidity is the term generally applied to the firm whose balance sheet has deteriorated too far. The next step is insolvency. With the secular trend of excessive credit creation, increasing numbers of firms are becoming illiquid to the point where their competitiveness is being impaired. As an individual firm becomes illiquid, it becomes less able to withstand external shocks, less able to adapt to changes, less able to compete internationally and becomes increasingly sensitive to business and credit cycles. As more attention must be devoted to managing the firm's debt, the management has less time

and inclination to devote to future planning and investment. Consequently, it gradually falls behind competitors. As its debt load grows, it falls increasingly at the mercy of credit markets. Finally, when accounts receivable and outstanding debt are rising even faster than sales, even the novice security analyst would take note. When this situation is multiplied by thousands of firms an alarm should be signaled for the entire economy. This is precisely the state of the corporate sector today.

"Over 70 percent of the government's expenditures are now uncontrollable without major changes in legislation."

THE AGGREGATE EFFECTS OF CORPORATE ILLIQUIDITY

The aggregate effects of corporate illiquidity are similar to those of the individual firm. As illiquid firms proliferate, the entire corporate sector becomes more vulnerable to external disturbances. It becomes more prone to a business slowdown and recovers in a more labored fashion. In the aggregate, the growing financial leverage has resulted in more volatility in the entire economy. More importantly, the declining corporate liquidity places an inexorable upward pressure upon interest rates in a number of ways. First, the increasing risk of corporate collapses must be balanced by higher interest returns. The greater volatility resulting from general illiquidity offers another portfolio risk to the investor for which he must receive compensation in the form of a higher interest rate. Secondly, the periodic scrambling for funds among growing numbers of illiquid firms during credit crunches also exerts a strong upward pressure upon interest rates. The postwar pattern has become quite predictable. In each business expansion, corporations incur excessive short term debt. As business begins to slow, they become concerned and rush to fund the short term debt by selling bonds. This only hides the short term excesses in another section of the balance sheet away from the very visible short term section. The excesses have been accumulating, however, and are increasingly manifested in higher debt ratios and lower interest coverage ratios. These, in turn, are reflected in growing number of rating cuts on the corporate securities. Finally, liquidity deterioration is inflationary in the shorter term and this adds a further inflation premium to interest rates.

To a firm that is top heavy in debt, rising interest rates can be fatal. Thus, we can see the first of many self-enforcing aspects of the liquidity deterioration. Illiquid firms are heavily penalized by the very interest rates that they are instrumental in raising. This is one of the many reasons why the trend of excessive credit creation and its effects are rapidly accelerating. The growing corporate illiquidity represents a latent deflationary force in the economy that can only be offset by ever larger doses of credit which, of course, enforces the trend. The economy is now in need of a massive rebuilding of capacity to atone for many years of underinvestment that may also be traced to the inflation that resulted from excessive credit. The enormous financing requirements of such an undertaking will be the final straw.

BANKING LIQUIDITY

Banks were both willing and able to supply the credit necessary to support the long deterioration in corporate liquidity. Following the lead of the government, the banking system has gone full circle. From the 1930's, when the government could not force banks to grant loans, the balance sheet of the banking system has reached a condition where it is far worse than the 1920's by any traditional measure of safety and liquidity. The steady deterioration since World War II has been interrupted only by short and partial cyclical restorations of liquidity. Since the liquidity scare of 1969-1970, there has been no recovery at all.

The climate fostered by the government has created a new banking philosophy. Banks no longer wait passively for deposits and then structure for balance between safety and earnings. Such high safety buffers, they say, are no longer needed. They can compete in the market place to determine their own deposit levels. The amount of loans is limited only by their ability to raise deposits, not by antiquated standards of safety. Thus, the percentage of assets in loans as well as the length of such loans has increased dangerously. One flaw in their reasoning, of course, is that what is possible for one bank is not possible for the entire system. Hence, the struggle for deposits among banks only succeeds in introducing a greater note of volatility into the financial system. The deposits, due to the competition, are becoming more sensitive in the short term and more volatile. At the same time, the traditional self-liquidating loan has become a smaller proportion of the average loan portfolio. In their place are increasing proportions of less liquid term loans as corporations have gradually gone into debt to the banking system. So we have a situation where deposits are becoming shorter and more volatile while loans are becoming longer, riskier and less liquid. *This goes exactly counter to advice usually given by the banker to his customer to avoid borrowing short to invest long.*

As loan demand rises sharply during cyclical upswings, the banks must aggressively compete for deposits at any cost and by any means since they have no unused capacity. This activity pushes interest rates higher, forcing banks to push for higher returns to cover the higher cost of funds. This search leads the banks to higher risk loans and investments. The gradually lengthening maturity of their loan portfolio also tends to lock in the higher costs and thus the level of interest rates in the system. Thus, banks have also added to the upward pressure on interest rates, increased volatility and risk in the economy. Through their money-creating function they have also added to inflationary pressures.

The deterioration of the banking balance sheet is so severe that only a huge liquidation of credit would restore normal liquidity relationships. Given the unwieldy debt load of corporations and individuals and the precarious financial condition of both sectors, such a credit liquidation would become cumulative. *Banks have no choice but to continue to help their clients become more deeply mired in debt in order to keep the system from collapsing.*

THE ROLE OF THE GOVERNMENT AND THE FEDERAL RESERVE

If banks did not create the necessary money and credit, the liquidity trends could not continue. Banks, in turn, could not supply the credit if the Federal Reserve did not supply the reserves. Therefore, the Federal Reserve does have a major supporting role in the problem. We must look first, however, to the government to find the prime mover.

The philosophy of small government, as mentioned, began to disappear in the 1930's. It was the huge buildup of liquidity during the Second World War and the pent-up demand, however, that provided the springboard for the postwar boom. Until 1951, the Federal Reserve was engaged in pegging the rate on government securities at artificially low levels creating even more excessive money in the process. From this condition of excessive liquidity, pent-up demand and the incipient belief in a large benevolent government, the long postwar boom and liquidity rundown began.

Although liquidity levels began to reach more normal levels in the 1950's, the growing government spending programs helped to perpetuate the deterioration. Programs, once begun, assumed a bureaucratic life of their own and consumed increasingly more funds even beyond the dreams of the original planners. Politicians, getting into the mood, vied with

each other to bring their constituents more programs. The budget became gradually less controllable.

On top of this, the New Economists finally came to full power. They came with theories and aspirations developed over the Eisenhower years and before in universities across the country. The original Keynesian theories were expanded. Under their guidance, the deterioration in the national balance sheet was accelerated. Even the Vietnam War did not deter them in their goals. Money was spent on *both* guns and butter as huge nondefense spending was added to the expenses of the longest war. Fiscal discipline was finally lost completely and deficits grew to astronomical heights as the government sector rapidly encroached upon the private sector. This spending, of course, had to be financed and this is the cue for Federal Reserve to enter the picture.

Taxes have certainly risen substantially in the postwar years financing a large part of the government debt. If this method of finance had been followed exclusively, the long deterioration in private balance sheets would have been greatly reduced. The government, however, would have been spending an even larger part of each dollar. But raising taxes has always been much less popular with politicians than the invention of new spending programs. Hence, an ever greater proportion of the debt was financed by government securities. The Federal Reserve, in its role of faithful handmaiden to the Treasury, purchased all the securities that were not taken up by the private sector, issuing high-powered money in payment. These reserves, multiplied manyfold by the eager banking system, supplied the means for the liqudity deterioration among corporations and individuals. Banks today generally loan or invest almost all of any increment to deposits.

In addition to aiding the Treasury financings, the Federal Reserve has also stimulated excess credit growth because of conflicting *goals* it has taken upon itself over the years in the spirit of the New Economics. While pursuing conflicting goals of full employment and stable prices, it has always erred on the side of inflation. Finally, the Federal Reserve has for years also pursued conflicting *targets*. It has fought valiantly to hold down interest rates but has lost control of the money supply time and again in the process. In the long run, the inflationary result of such excessive money growth has served to place further upward pressure upon interest rates in one more example of the self-enforcing nature of the postwar credit trends.

Thus, we see that the government and the Federal Reserve have teamed up to create not only a climate favoring excess credit growth but have also created excessive monetary growth over the postwar period to make it possible. The correlation between excessive money growth and price inflation has been well-documented just as the relationship between inflation and interest rates has been established.

"The chances of a financial panic at any time are great . . . the collapse can be worse than the 1930's, for credit has permeated the entire economy."

Now that the actors have all been introduced we can see the full explanation of our current financial problems. Banks, corporations and individuals have all run down their balance sheets over an extended period of years aided and abetted by the government and the Federal Reserve. The primary results have been inflation, rising interest rates, increasing volatility and a growing risk of total collapse. Although the primary blame rests upon the government, as the effects become persistent they interact to form a self-enforcing upward spiral that becomes more difficult to break as time passes.

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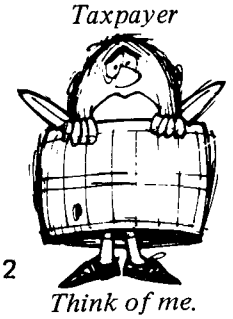

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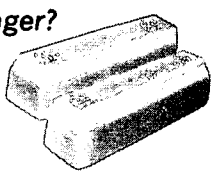

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Many nostrums have been applied but to date, no one has attempted to break the chain at the root of the problem.

CAUSES AND EFFECTS

One reason the chain has not been broken lies in the fact that the credit deterioration has been allowed to persist for such a long time that the primary effects mentioned above have become deeply engrained in every sector of the economy. They have so permeated the system that many secondary effects such as lower capital formation, declining productivity, declining profitability, increased labor militancy and shortened investment horizons have also taken hold. Labor unions have learned to protect their *real* wage with proliferating cost-of-living clauses, for example. Along the way, all the restraints on the ability of the Federal Reserve to increase the money supply, such as the gold cover, have been removed by necessity. Through the fixed exchange rate system, our increased money supply and the resulting inflation have been exported throughout the world. International crises and the scrapping of the old international monetary system have resulted. The Keynesian system is a "closed system" and did not anticipate this development. All these effects have been intertwined and work to enforce each other into an independent self-enforcing trend of liquidity deterioration. In many cases, the effects are confused with the cause: business blames labor, labor blames big business, scapegoats like multinational companies, the gnomes of Zurich and others are singled out. Yet, the underlying government spending and money creation continue unabated.

As further evidence of people's ignorance of the basic causes, controls on prices and wages have spread throughout the world. The result has been loss of economic and personal freedom but little reduction in inflation. Controls, in turn, lead to shortages and declining incentives to invest by the private sector. This results in lower capital formation, lower productivity and further shortages. Inflationary pressures are thus worsened and the United States is now importing the inflation in the form of higher commodity prices which it exported earlier. The self-enforcing upward spiral continues as long as the underlying causes are neglected.

SOLUTIONS

An obvious solution would be a reduction in government spending and enlargement of the private sector. The growth of credit must also be reduced to a rate not exceeding the rate of potential growth of real goods and services. Nothing less than a complete reversal of government philosophy will solve the problem. The entire credit ethic that has mushroomed in the postwar years must be changed. Finally, a long period of slower growth and higher saving and investment to offset the long stimulation of consumption at the expense of investment is needed.

There is a very important question as to whether any politician in the free world has the will to order or vote for the changes that would be necessary to solve the problem. In the United States, the budget is already out of control. Over 70 percent of the government's expenditures are now uncontrollable without major changes in legislation. It is difficult to imagine many Congressmen willing to vote out Social Security, veterans' benefits, welfare and other deeply engrained government programs. Controlled inflation has always been a favorite government tool but now control is being lost.

Like the large dollar overhang in the world, the level of debt already outstanding may be so large and the credit ethic so deeply engrained that *token* changes in government policy will not be enough to stop the trend. On the other hand, if a sufficiently large decline in credit growth is attempted, it would set off a cumulative liquidation of credit that will also get out of control. Just as the creation of credit takes on a self-perpetuating nature, the liquidation will do the same. We simply cannot reduce the credit base too rapidly. To avoid a crisis, the debt can only be eliminated slowly, over a long period of time. This will require close cooperation between all branches of government over several administrations, which seems too much to expect. Each time the government has attempted to slow credit in recent years (e.g. 1969-1970) it finds it cannot without the situation getting out of hand. It then quickly reverses itself and must feed out even more credit to turn the economy around which sets the stage for further credit growth and the next credit crunch. The government has a tiger by the tail. It is afraid to let credit grow too much but at the same time it must supply increasingly larger doses of credit to offset the deflationary pressures that are growing from increasing numbers of illiquid firms.

HOW WILL IT END?

The chances of a financial panic at any time are great. Contrary to much current thinking, the collapse can be worse than the 1930's, for credit has permeated the entire economy. Not only the speculator will be hurt but most private citizens as well. All panics in the past have been caused by credit liquidation but the credit binges preceding the past panics had been relatively short and speculative in nature. We have now engaged in a much more respectable 30 year credit binge where the average citizen and corporation has participated fully with the blessing of the government. This time, the binge has taken the form of mortgages, auto loans and other consumer debt. Corporations have become much more highly leveraged than at any time in the past and banks have become more illiquid. Anything could trigger the liquidation of this huge credit base whether the near-miss of the Penn Central or an Arab oil embargo. Once started, the trend will gain momentum in spite of government efforts to halt it.

Can the government continue to put off the inevitable? We should never underestimate the power of the politician and his skill in crisis economics. The hour is late, however, and to the extent that the government is successful, the side effects will continue to worsen. The price to be paid is more credit extension, inflation, volatility, rising interest rates and a continued loss in personal and economic freedom. Balance sheets are now so weak that they constitute a separate force that must be reckoned with by the government. Increasing doses of credit will be needed, crisis economics will continue, and shortages will periodically emerge as the government attempts to supplant the law of supply and demand. Worsening credit crunches and international disruptions will also be the rule. Eventually, control will be lost completely and either inflation will spiral as in Germany after World War I followed by a crash or a crash will be triggered before then by some yet unknown event.

WHAT TO DO

The task of protecting one's investments will be difficult in the years ahead. The investor must keep the possibility of a crash in mind while at the same time he must reckon with the government's ability to patch things up and put off the eventual end. The side effects could continue and investments that one may choose for a crash can suffer substantially in the interim if inflation accelerates. It is simply difficult to hedge against *both* inflation and deflation at the same time. If one were sure the crash was imminent, cash, gold and high quality bonds would be excellent.

Until the crunch, however, inflation will continue to be the primary evil. Cash could become worthless before the crash finally comes. In the meantime, choppy business cycles and frequent credit crunches will be the rule. Rising interest rates would make long term bonds a poor investment. The only solution is to structure portfolios judiciously between short-term fixed investments, gold investments and high-quality equities with strong finances and the ability to offset inflation. ◻

WOULD YOU TRUST YOUR LIFE TO THIS MAN?

Unless you already live on a self-sufficient farm, I'm afraid there's no way you can avoid it. And most of the Libertarians I know are still going about their business as though the problem were as abstract as their favorite mode of mental activity. Unfortunately but nevertheless obviously, the Causes set in motion by the character above will soon bear their effects.

According to the finest minds, simple arithmetic and raw logic, we are about to witness the terminal stages of what Franz Pick calls "currency cancer". The Bureau of Labor Statistics reports that wholesale prices rose in January at a seasonally adjusted annual rate of 37.2%, with food, farm products and feed leading the way with 61.2%!

Consider also the "unfortunate" error by Mr. Butz regarding a 170 million bushel wheat surplus to tide us over until the summer harvest: the Ohio Bakers' Association reports that these same U.S. Dept. Agriculture figures actually reveal a 900,000 bushel shortfall, which could result in a serious bread shortage in May if certain nasty things are not done to our overseas wheat customers.

Are you sure you're not trusting the incompetent sir above **more** than you realize?

Assuming you lack psychic powers, you will be able to precisely anticipate neither the timing nor the full impact of events increasingly beyond your control. Consequently, you must provide an ever-widening margin of safety as gyrations from the norm become more and more extreme, and the situation more and more vulnerable, more psychologically fragile.

By now, hopefully, you have realized some gain from your hard-money investments. Have you considered what true value these will have if the worst actually happens? Can you deal with the kind of disruption caused by strikes and shortages of basic commodities? Do you expect to be able to resist political blackmail and insure the spread of superior political ideas in the midst of such disruption? Are you, in effect, trusting your life to the Man?

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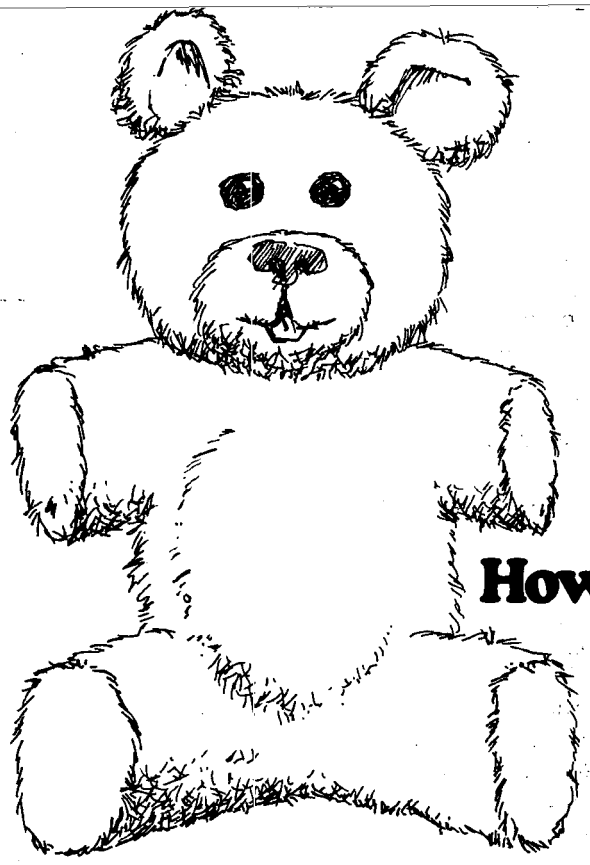


How to have fun in a bear market

Thomas J. Holt

Most investors will agree, in retrospect, that a major bear market has been in progress since year end 1968. Certainly, most stocks are now selling far below their 1967-68 peaks. Although many bear market rallies have already taken place and many more will occur in the future, there is little doubt that the ongoing primary bear market will persist beyond the mid-1970's. The world economy has yet to undergo a sizable and lengthy correction.

But there's no real reason why investors should shy away from bear markets. Of course, it's no longer possible to simply buy any stock and let the bull market drive the price up. Trading on "hot tips" and rumors will also prove expensive. But *bear markets may actually offer many extra profit opportunities that would not be available otherwise* — to systematic individuals.

CASE STUDY. Let's take a hypothetical situation where two investors are interested in buying stock in a growth company selling at, say, 50. Although the issue, having risen sharply, is richly priced relative to earnings and assets, Investor A decides to buy it immediately because he is impressed with the company's long-term prospects. Investor B, however, holds back, convinced that a primary bear market is unfolding and that high-priced stocks usually suffer in such a drop.

During the course of general market decline, the hypothetical stock drops to 30. Investor B buys it at this point. With the same amount of capital, Investor B, by taking advantage of a bear market, is able to buy two-thirds more shares of this growth situation. If the stock recovers to 40, Investor B will have a 10-point gain, as against a 10-point loss for Investor A; and if the stock eventually rises to 60, Investor B will enjoy a 100 percent appreciation, or five times more than Investor A's 20 percent gain.

However, the chances are that Investor A will not hold the stock through the decline to 30 and subsequent runup to 60. As the bear market progresses, he will become increasingly anxious and more likely than not bail out in panic near 30. If he holds, he's apt to get out as soon as the stock approaches 50 on its way back up.

Perhaps the most important part of successful strategy in bear market investing is to have a sufficient cash reserve with which to buy *real* bargains created during the course of a general market decline. This is so elementary many readers may wonder why we bother to discuss it seriously. The fact is, however, that after 20-odd years of rising stock prices that persisted through the mid-1960s, many investors still become restless holding a fraction of their investment capital in cash for even a few days, let alone hanging on to sizable reserves for weeks or months. For the venturesome, potential buying power can actually be increased in a bear market by using hedges and shorts.

NEW APPROACH

To take profitable advantage of a primary bear market, it behooves the investor to learn and follow the dozen bear market guidelines set forth herewith:

1. **Don't sit tight.** Hanging on to "good" stocks "for the long pull" and riding through an

Thomas J. Holt is the president of New York-based T. J. Holt & Co. which publishes THE HOLT INVESTMENT ADVISORY *and manages investment portfolios for private investors. Mr. Holt holds college degrees in economics and engineering.*

interim market decline may have proved reasonably satisfactory during the long bull market when the primary trend of most issues was upward. But in a primary bear market, such a course of inaction will prove most impractical and nerve-wracking. Take, for instance, the leading steels like Bethlehem and U.S. Steel, which, for reasons peculiar to that industry, have endured their own private bear market since long before the general decline set in. These issues have trended downward for about a decade and there is little evidence to suggest that shareholders will improve their lot by hanging in there for another few years.

2. **Don't look at past highs.** Even investors who have every intention of liquidating overpriced stocks often fail to do so because they are waiting for their holdings to return to the peak levels attained during the height of the speculative spree. In all probability, those high water marks may not be reached again for many years.

3. **Don't worry about taxes.** One of the more common reasons why many long-term investors don't realize the capital gains they have accrued during the course of a long bull market is their reluctance to pay capital gains taxes. Important though they may be, tax considerations should never come before investment merits. It is often far cheaper to pay a tax of roughly 10 percent to 25 percent on only the capital gains than to run the risk of a much larger loss on total capital. This is particularly true in the case of overpriced issues.

Actually, as soon as a stock advances from purchase price, a potential tax liability accrues. It can be removed either by nailing down the profit and paying the taxes or having the stock retreat to or past the original purchase price, thereby eliminating the paper profit. Obviously, the first alternative is the more pleasant.

Another way of looking at the "frozen-in-by-taxes" situation is to consider the tax liability more or less as an interest-free margin debt. While it is good to use other people's capital, interest free, it is not advisable to resort to margin to buy stocks during a primary bear market.

4. **Do capitalize on technical rallies.** Even during major bear markets, there will be occasional rallies. Some will last several months; others, only a few hours.

The short ones afford excellent opportunities to move out of weak issues. Once again, this rule seems almost too elementary to be worth the stating. However, many investors who intend to sell during the "next" rally often forget their plans as soon as the market makes a strong advance. In response to the market's interim move, their mood changes from one of panic to euphoria and they miss out on good selling opportunities.

The major cause for such emotional shortcomings usually lies in the fact that such investors don't have strong convictions about their investment (or divestment) programs. To be convinced, the private investor must be informed not only about the stocks involved but also about fundamental conditions in the market, the economy, and the monetary system.

Longer bear market rallies, meanwhile, can generate excellent trading profits for the nimble. To take advantage of these rallies, investors should buy stocks only *after* the market has plunged precipitously for a few months and stocks are technically sold out.

To check if such a truly oversold condition has been reached, check the sentiment of stock brokers and market commentators. When they are worried but are still looking for an imminent recovery, don't buy. But when they sound downright discouraged and begin to talk seriously about depression, start accumulating stocks that have undergone sharp declines.

5. **Don't give up investing.** In a primary bear market, it is of course safe to simply withdraw from securities markets altogether. But a systematic program of building capital requires an efficient use of funds, and noninvesting is decidedly inefficient. Money can always be put into something other than overpriced common stocks. To cite but one simple example: hedging with warrants and convertibles can be highly rewarding, yet involve limited risks.

6. **Don't buy mutual funds.** The great majority of mutual funds are bull market creatures. They are accordingly apt to suffer far sharper declines than the market in general.

7. **Do select truly "defensive" stocks.** When they expect a market decline, many investors instinctively think of buying utilities, or other so-called "defensive stocks." Following this instinct blindly can prove costly. To the extent that these companies are unlikely to go bankrupt — even if a severe recession occurs — or that their earnings do not

fluctuate very widely, they can be considered defensive. But unless a given issue is reasonably priced in relation to existing and probably capital market conditions, it's just as vulnerable to price declines as any other.

Truly defensive stocks in today's market are those issues which offer a high and reasonably safe dividend return. If the current yield is higher than the average interest rate of three to five year government bonds, the stock is usually suitable. Investors are becoming so much more income-minded now that high-yield stocks will sooner or later attract their attention.

8. **Don't buy low P/E stocks willy-nilly.** Premature bargain-hunting is a very dangerous game. In the all-time worst bear market — the 1929-1932 crash — the most staggering losses were incurred not in the initial slide but during the period thereafter.

One of the most common mistakes made by investors is to rush into stocks simply because current price/earnings ratios are lower than the average multiples of the recent past. P/E ratios are not a good investment yardstick. Since 1961, for example, A.T.&T.'s earnings multiple has declined markedly. But there are few shareholders who have bought the stock during the past decade who don't have a paper loss.

9. **Do consider bonds.** Investing in bonds has not been a particularly profitable proposition during most of the past quarter of a century, when interest rates were trending upward. But before too long, interest rates are more likely than not to move downward. When that happens, long-term bonds will offer appreciation potential as well as generous income.

It's true that bonds do not "swing" quite as feverishly as common stocks. But the enterprising investor can still come out well ahead in such securities. For example, with interest rates likely to be much lower in the mid-1970s, many bonds will probably appreciate significantly in the next several years. There will, of course, be short periods of reverses, which long-term investors may ignore.

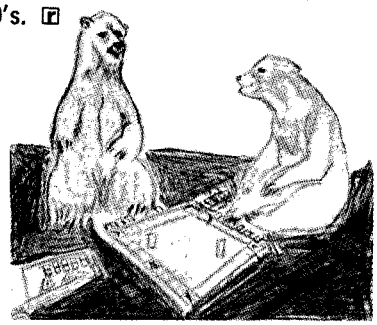
10. **Do buy gold stocks.** The ongoing bear market will be accompanied by a weakening of the economy. And politicians can be expected to respond by "printing" more and more paper money. This cannot help but increase the price of gold — the only time-honored standard of value. Gold stocks will rise in sympathy, especially since demand for the limited number of these shares will almost certainly broaden all around the world.

11. **Do seek out special situations.** Even during business recessions, there'll occasionally be certain companies that will keep on growing. And if their stocks are not overpriced, they can reasonably be expected to give investors a run for their money while a primary bear market is under way. But even should they hit temporarily, they are likely to recover vigorously once selling subsides.

Right now, for example, some of the senior bonds of bankrupt railroads operating in the Northeast are highly attractive. The assets behind these securities are worth far more than face value of the bonds and many of the bonds are selling at but a tiny fraction of their face value. The new law authorizing the forming of a government-sponsored railroad system to take over these bankrupt roads promises excellent treatment of these bonds in the final reorganization.

12. **Do use selected short sales.** Generally speaking, selling short is highly risky. But in a bear market, this technique can be put to good use. Indeed, shorting overpriced stocks can be safer than buying even blue chips.

Thus, a bear market need not spell defeat for the sophisticated investor. By following these 12 guidelines, you stand a good chance of coming out ahead — and even having fun — in the bear market of the 1970's. ◻



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4. We don't just try to beat the averages. In a declining market, investors find little comfort in knowing that they have lost less than the Dow or the S&P. Our clients want to protect and build their capital in a down as well as an up market, and our efforts are directed toward helping them achieve that goal.

5. We pay careful attention to international monetary developments and to the domestic flow of investment funds. Ever since late 1967, for instance, we have alerted investors to the gradual disintegration of the international monetary system and the inevitable rise in gold and silver prices. What's happening abroad, in our opinion, has a strong bearing on the economic prospects at home.

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6. We don't give one-sided recommendations. All too often, investors are told when to buy but not when to sell. To avoid that situation, every security recommendation made by our Advisory comes in two parts. For every "buy", there is a subsequent "sell". For every "short", there's a subsequent "cover". Until the second part of each recommendation is made, open positions are reviewed through periodic follow-up reports.

7. We don't try to insult investors' intelligence. When we make mistakes—yes, we do make them—we don't blame them on Watergate, the energy crisis, or whatever. Nor do we sweep under the rug our bad recommendations.

As a matter of fact, to our knowledge The Holt Investment Advisory is the only service in the industry that always makes available to anyone, upon request, the complete performance record of all security recommendations ever made. The summary of that 7-year record is regularly published in the Advisory every month.

8. We believe common sense is more important than outdated conventions. Blue-chip growth stocks are supposed to be safe investments. But we cannot see how in recent years buying blue chips that sold at lofty earnings multiples and provided hardly any dividend income could be construed as prudent investing.

On the other hand, we have advocated some short selling since late 1971. Wall Street convention considers short selling reckless. But common sense tells us that in a long-term bear market, most stocks are more likely to go down than up. We therefore believe that in such an environment, shorting overpriced stocks is less risky than buying blue chips.

9. We practice the Total investment approach. In addition to common stocks, we think such securities as warrants, convertible debentures, corporate and Government bonds and Treasury bills can sometimes be attractive investment vehicles. The enterprising investor could also benefit from investigating the merits of hedging and leveraging.

Our Total investment approach also incorporates flexibility. Instead of being either 100% invested in equities or holding all cash, we allocate various portions of investment funds to various securities and techniques. And we adjust the portfolio composition whenever necessary to reflect changing market conditions.

10. We believe in the power of positive investing. We submit that with a little imagination, some common sense and a lot of knowledge and conviction in what he is doing, every investor can strive to protect and build capital in both bull and bear markets.

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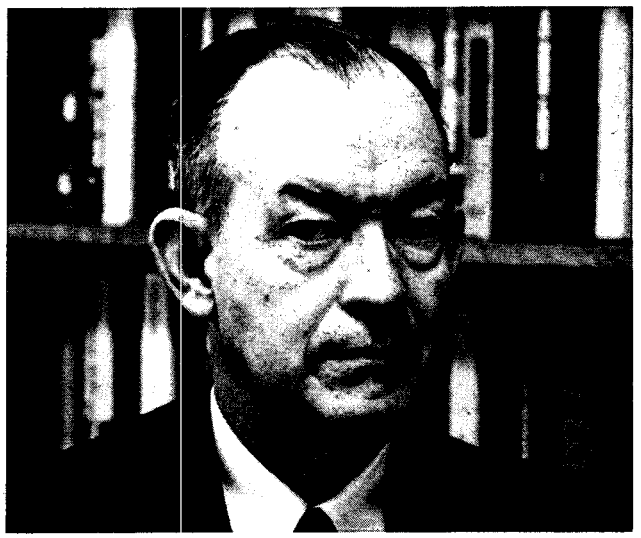
THE DOW THEORY REVISITED

George Bishop

From late October through December of 1973 stock prices persistently declined. The Dow Jones industrial average, which stood at 980 in October, fell below 800 in November. During the same period the Dow Jones transportation average fluctuated within a narrow range. Toward the close of the decline in the industrial average, investors noted that the financial press and current periodicals mentioned the "Dow Theory" in many of their stock market articles. A number of readers who scanned references to "confirmation" of the Dow Jones averages and "divergence" between the industrial average and transportation average must have wondered what the Dow Theory was all about and its degree of usefulness to those engaged in equity investment and speculation.



Professor Bishop holds the A.B. degree in History from the College of William and Mary and the M.B.A. and Ph.D. degrees from New York University. He had an extensive business career, which included twelve years employment with Merrill Lynch, Pierce, Fenner and Smith. He taught finance at the University of Tennessee, Knoxville, Tennessee, from 1959 through 1964. Since September 1965 he has been Professor and Chairman, Department of Finance, Northern Illinois University at DeKalb, Illinois. Professor Bishop is the author of CHARLES H. DOW AND THE DOW THEORY; *editor of* CHARLES H. DOW: ECONOMIST; *a contributor to* COLLIER'S ENCYCLOPEDIA *and* THE ENCYCLOPEDIA BRITANNICA, *and author of many articles in the learned journals and popular publications.*

The Dow Theory as known and discussed in financial circles today is actually the result of a long evolutionary process, consisting of a number of milestones. The first of these was the contribution of Charles H. Dow (1851-1902) to stock market theory.

Dow was one of the foremost financial journalists of his time. In him we find no financial visionary evolving a Monte Carlo system of beating the stock market, but a newspaperman of the highest standing who learned his trade under the leadership of Samual Bowles, one of the newspaper giants of all time. Dow's writings in *THE WALL STREET JOURNAL,* of which he was founder and first editor, showed a firm grasp of economic theory, domestic and international banking, corporate financial practices, financial and economic history, as well as stock market theory and practice. His work on the *JOURNAL* firmly established his reputation as a financial journalist. He is also generally given credit for compiling the first average of stock prices.[1]

THE WALL STREET JOURNAL first appeared on July 8, 1889, with Dow as editor, and has been a part of the financial scene ever since. Dow's many paragraphs appeared in the paper until shortly before his death on December 4, 1902. In conformity with prevailing newspaper practice, Dow did not identify his writings. However, it is possible to establish the identity of his writings for the period April 21, 1899, to October 25, 1902, inclusive.[2]

Dow's editorials covered many subjects. His views on the business cycle were advanced for the times and there is no doubt much of the later theoretical interpretation of business cycles developed by economists drew basic data and support from the daily writings of Dow and other early financial journalists.[3]

There is a very strong possibility that Charles H. Dow did not formulate a stock market "theory" as such. Dow's editorials embraced many subjects, with investment and stock market speculation prominent among them. It is, of course, impossible to learn to what extent Dow's readers looked upon his editorials as setting forth a stock market theory. The editorials were almost a daily feature of *THE WALL STREET JOURNAL,* and no doubt greater emphasis was placed on certain editorials by some readers who, in turn, gave less attention to others. Those editorials which contained suggested

methods of trading in stocks probably acquired a following.

"DOW'S THEORY" EMERGES

In 1902 Samuel Armstrong Nelson added *THE ABC OF STOCK SPECULATION* as Volume V in Nelson's Wall Street Library, a series of books concerned with the stock exchange.[4] Nelson had endeavored to have Dow write the book but his efforts were unavailing. As a result he undertook the work himself, using selected editorials written by Dow, and previously published in *THE WALL STREET JOURNAL,* as the basic framework for the book. Of the 35 chapters that comprise *THE ABC OF STOCK SPECULATION,* 17 consist of editorials written by Dow, and 15 of these chapters were designated by a footnote as "Dow's Theory." Evidently, this was the first use of the term in print. Thus, the Dow Theory was originally named in footnotes incorporated in a work on speculation in common stocks, hardly an auspicious beginning for an appellation that has endured in the language of the market place to the present day.

In this manner S. A. Nelson first named the theory, and was the first "Dow Theorist" in print. However, Nelson cannot be classified as an exponent of the Dow Theory—other than for his role in the selection of Dow's editorials—since he did not add by way of interpretation to the words of Dow.

The editorials selected by Nelson contained many principles that could be utilized by investors and speculators engaged in investing and trading in common stocks. Dow advised his readers to be conservative, to avoid buying on margin in larger amounts than prudent considering their resources, and to have an idea of the value of the stocks they purchased. In this last respect Dow wrote along the lines of what today is classified as security analysis.

For the stock market trader, Dow discussed the maxim—"Cut your losses short, but let your profits run"—and the placing of stop orders. He likewise devoted many paragraphs to the two general methods of trading in stocks, namely, trading in relatively large amounts coupled with the use of stop orders and buying on a scale down, or averaging purchases as a stock declines. It should be noted that this is not the same as dollar averaging.

However, Dow's contributions to stock market thought by his classification of three movements in the market and the formulation of the law of action and reaction no doubt caused a great deal of discussion among the readers of Nelson's volume. Dow stated there were three movements in the market—all going on at the same time. The first was the daily fluctuation; then the short swing ranging from about 10 to 60 days, and finally the main movement covering at least four years in duration. Dow was a firm believer in the periodicity of the business cycle and felt that the first action of a trader should be to ascertain if a bull or bear market was underway. This was reflected, of course, by the direction of the main movement over an extended period of time. As an aid in determining the main movement, Dow developed the famous "Dow Jones Averages."

The law of action and reaction applied to movements in individual stocks as well as the general equity market as reflected by a stock average. It was a rule that a primary move would have a secondary movement in the opposite direction of at least three-eighths of the primary movement. Apparently both the concept of the three movements in the market and the law of action and reaction were original with Dow.

"There is a strong possibility that Charles H. Dow did not formulate a stock market 'theory' as such."

Shortly after the publication of *THE ABC OF STOCK SPECULATION,* S. A. Nelson died and the book went out of print. It was only republished at a much later date, but remained available in libraries and secondhand bookstores.

A THEORY OF FORECASTING

The first great exponent of the Dow Theory, William Peter Hamilton, next appeared upon the scene. He was a Scottish journalist who served as editor of *THE WALL STREET JOURNAL* from January, 1908 until his death on December 9, 1929. Hamilton joined the staff of the *JOURNAL* in 1899 and worked under Dow's editorship until the latter's death. There is no proof that Hamilton was ever a close associate of Dow, as many writers hold; rather, the evidence indicates that their relationship was that of employer and employee and editor and reporter. He presented his version of the theory not only in *THE WALL STREET JOURNAL* but in *BARRON'S* and in a book, *THE STOCK MARKET BAROMETER,* published in 1922. From that time until his death Hamilton was looked upon as the leading exponent of the Dow Theory.

The Hamilton version of the Dow Theory is the "Dow Theory" known and discussed in financial circles today. In short, Hamilton presents the view that prices on the stock exchange take account of all known facts and discount business conditions. The Dow Jones averages are representative of stock exchange prices and hence discount business conditions. Hamilton also stressed the "confirmation of the averages" and the action of a "line formation" in the averages.[5]

Dow saw the stock market as a part of the entire economic system and approached the problem of investing and trading in common stocks by a study

of current economic conditions, an analysis of the position of the general equity market and of individual stocks within the market, as well as a financial analysis of the corporations concerned. Hamilton, however, extended the general observations of Dow into a theory of *forecasting* both the stock market and economic events. It is important to note the transition from the principles and rules on speculation and investment approach as presented by Dow to the forecasting approach of William Peter Hamilton.

"Hamilton extended the general observations of Dow into a theory of forecasting *both the stock market and economic events."*

After Hamilton's death no advocate of the Dow Theory came forward to command recognition until Robert Rhea published a series of articles on the subject in *BARRON'S* in 1932. That same year Rhea published *THE DOW THEORY* which canonized Hamilton and firmly established the Hamilton version of the Dow Theory as standard. Rhea's volume, with its keen analysis of Hamilton's editorials, did much to revive an interest in the theory which had suffered an almost fatal thrust by the general disillusionment that accompanied the deflation of the bull market in the years 1929-1932.[6]

From 1932 until his death in 1939, Robert Rhea was looked upon as the leading exponent of the Dow Theory and there is no doubt he did much to popularize and publicize it. His stock market service published a series of letters entitled *DOW THEORY COMMENT* in which he traced the performance of the Dow Jones industrial and railroad averages and discussed the various movements with respect to the primary and secondary trends of the market. The *DOW THEORY COMMENT* letters reached 6000 subscribers.

Rhea's book, *THE DOW THEORY,* takes the form of a manual or a compendium in which Rhea compares quoted portions of Hamilton's editorials, or passages from *THE STOCK MARKET BAROMETER,* with the various tenets of the Dow Theory. Rhea's original contributions are at a minimum, but they are very effective when they appear. His great contribution to the Dow Theory is the manner in which he sets forth the tenets in a single listing and clearly defines each concept; his primary achievement is one of classification. There is no doubt that he performed his declared task, that of formulating the Dow Theory, through a study of the writings of Hamilton in a competent manner. As for the work of Charles H. Dow, Rhea was not really familiar with it, and he made no pretense to the contrary.

Any attempt to fuse the writings of Dow and those of Hamilton and Rhea into a concordant theory presents many difficulties. It must be remembered that Dow was a journalist writing timely articles on matters that were of current interest to his readers. Hamilton, however, in *THE STOCK MARKET BAROMETER,* and Rhea, in *THE DOW THEORY,* presented a formalized theory of market forecasting.

In short, the evolution of the Dow Theory consisted of four steps: first, the original editorials of Charles H. Dow; second, the compilation by Nelson of Dow's editorials in *THE ABC OF STOCK SPECULATION;* third, Hamilton's emphasis on the confirmation of the averages, line formations in the averages, and the use of the action of the market as a forecasting device; and fourth, Rhea's acceptance of the Hamilton version of the Dow Theory and his placement of the various tenets of the Dow Theory in definitive form.

THE DOW JONES AVERAGE

Dow's compilation of an average of stock prices in 1884 was one of the great contributions to stock market methodology. Dow computed the average, or the arithmetic mean, of stock prices by adding the prices of the stocks included in the specific average, and dividing the figure by the number of stocks so used. He did not use a weighted mean, or make adjustments of any other nature. There is no evidence that Dow looked upon the averages as containing anything more than an indication of a statistical nature of the trend of the stock market as a whole. It was for this reason that Dow found it desirable to include "active" stocks (i.e., those stocks with a large volume of transactions) in the averages.

The Dow Jones averages remained averages, or arithmetic means, throughout Dow's lifetime. Therefore, he was not concerned with adjustments for stock splits as is the case with the Dow Jones averages today. Dow did substitute one stock for another in the averages and to this extent attempted to have the averages reflect the trend of the market under changing conditions.

The present Dow Jones averages are not averages but are indexes. The industrial average of 30 stocks began on October 1, 1928 and was calculated by adding the closing prices of the 30 stocks concerned and dividing by 16.67. This divisor was arrived at by adjusting for stock splits and stock dividends. A constant division was used for the first time on September 10, 1928 when the industrial average contained 20 stocks. Prior to that time an attempt was made to compensate for stock splits by applying a multiplier to the individual stocks concerned, i.e., the closing price of American Can would be multiplied by 6, that of General Electric by 4, etc. The divisor has been changed many times to adjust for stock splits and stock dividends since, and at the time of writing is 1.626.

The transportation average was introduced on January 2, 1970 and was devised to replace the railroad average. It includes the stocks of railroads, airlines, and other corporations concerned with the transportation industry. There are 20 stocks in the average and the divisor at the time of writing is 3.231.

The validity of the Dow Jones averages as a proper measure of overall market movements has been questioned due to the relatively small sample used. Two other criticisms often advanced are the lack of weighting by size of capitalization of the corporations concerned and the change of a stock's weight in the sample due to major changes in capitalization. Likewise, the substitution of stocks in the averages over time has also received critical attention.

Those who defend the use of the averages point out that the selection of the stocks in the averages is not a random one and the corporations included by their stock issues represent large businesses. As a result the averages do not include marginal concerns or special situations. Likewise, the Dow Jones averages are still the gauge of the overall market to a great number of investors and speculators and their long historical record makes it possible to use them for comparison purposes.

PREDICTION VALUE

Has the Dow Theory successfully predicted bull and bear markets making it possible for Dow Theorists to profit thereby? Evidence that this is the case has been accumulating for 40 years. Alfred Cowles III read a paper before a joint meeting of the Econometric Society and the American Statistical Association in Cincinnati, Ohio, on December 31, 1932. This paper was concerned with the stock market forecasting records of 20 fire insurance companies, 16 financial services, 24 financial publications, and the Dow Theory forecasting record of William Peter Hamilton from December 1903 to December 1929.[8]

With respect to Hamilton's record Cowles states:

> From December 1903 to December 1929, Hamilton, through the application of his forecasts to the stocks comprising the Dow Jones industrial averages, would have earned a return, including dividend and interest income, of 12 per cent per annum. In the same period the stocks comprising the industrial averages showed a return of 15.5 per cent per annum. Hamilton therefore failed by an appreciable margin to gain as much through his forecasting as he would have made by a continuous outright investment in the stocks comprising the industrial averages. He exceeded by a wide margin, however, a supposedly normal investment return of about 5 per cent. Applying his forecasts to the stocks comprising the Dow Jones railroad averages, the result is an annual gain of 5.7 per cent while the

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"In the history of stock market thought, Dow's place is of similar importance to that of Adam Smith in the field of economics."

railroad averages themselves show a return of 7.7 per cent.[9]

Justin F. Barbour in an article in *THE ANALYSTS JOURNAL* disputes the methodology used by Cowles.[10] He argues that had the period of study been from December 1903 to December 31, 1932 the return on a continuous investment would have been far less, and Hamilton's gains would have been substantially greater. Cowles was unfortunate in his selection of the period of time included in the study by concluding it with Hamilton's death on December 9, 1929.

Hamilton's famous "A Turn in the Tide" editorial appeared in *THE WALL STREET JOURNAL* on October 25, 1929 in which he advised his readers that the great bull market was over. Hamilton concluded in this editorial that "together the averages gave the signal for a bear market in stocks after a major bull market with the unprecedented duration of almost six years." Since Cowles' methodology assumed Hamilton sold short when he was bearish and covered only when he became doubtful or bullish it does not appear reasonable to assume that Hamilton would have covered his short position in December 1929, had he lived, considering the action of the averages during that month.

In 1944 Cowles continued his study on stock market forecasting and extended the records of 11 of the forecasters who had been the subject of his research published in 1933 in *ECONOMETRICA* entitled "Can Stock Market Forecasters Forecast?" Cowles did not identify the forecasters but states: "These organizations are well known. Names are omitted here because their publication might precipitate controversy over interpretation of the records. The wording of many of the forecasts is indefinite, and it would be frequently possible for the forecaster after the event to present a plausible argument in favor of an interpretation other than the one made by a reader."[11]

Cowles found that the forecasting agency with the most successful record for the period from 1928 to 1943 could be extended back to 1903. He explains as follows:

> While three individuals were for different periods responsible for the forecasts through these 40 years, the general principles followed by them all were similar and the succeeding forecasters were avowed disciples of their predecessors. It therefore seems justifiable to treat the combined record as a continuous one for the 40 years in question.[12]

Who were these three individuals? Justin F. Barbour identifies them as William Peter Hamilton, Robert Rhea, and Perry Greiner.[13] Therefore, the method used by these individuals was the Dow Theory as all are recognized as Dow Theorists. Recently Perry Greiner extended the forecasting records according to the Dow Theory to seventy years.[14]

We have revisited the Dow Theory and although the writer will not forecast what the future holds for it, he will repeat a thought he has previously expressed in print. In the history of stock market thought, Dow's place is of similar importance to that of Adam Smith in the field of economics. If this is so then the Dow Theory will be revisited time and time again in the future. ◻

NOTES AND REFERENCES

[1] For an account of Dow's life and work see George W. Bishop, Jr., *CHARLES H. DOW AND THE DOW THEORY* (Appleton-Century-Crofts, Inc. 1960).

[2] Dow wrote the "Review and Outlook" column in *THE WALL STREET JOURNAL* during this period.

[3] For a selection of Dow's writings on business cycles see George W. Bishop, Jr. (Ed.), *CHARLES H. DOW: ECONOMIST* (Dow Jones Books 1967).

[4] The book first appeared on December 24, 1902 and has been republished in several editions since that time. Dow did not live to see the completed work since he died on December 4, 1902.

[5] Confirmation of the averages means that when the Dow Jones industrial or railroad (transportation) average moves into new high or low ground the other average must do likewise for the movement to have significance. The Dow Jones public utility average is not considered. A "line formation" in the averages means a horizontal movement in both averages within a narrow range. The movement must continue for a number of weeks according to Hamilton, but he placed no limit on the extent of the range. Robert Rhea places the range at "approximately 5 percent" and places the time limit at "two or three weeks or longer."

[6] Rhea reprints as an Appendix in *THE DOW THEORY* a total of 260 editorials from the pen of Hamilton. Of these 212 appeared in *THE WALL STREET JOURNAL* and 48 were published in *BARRON'S.* They span the years 1903 to 1929, inclusive. Professor Henry B. Kline of the English Department in the University of Tennessee assisted Rhea in identifying the articles. Kline died in 1951.

[7] For a technical discussion of the construction of stock price indexes and criticisms of well-known indexes, including the Dow Jones averages, see *COMMON-STOCK INDEXES,* Cowles Commission for Research in Economics, Monograph No. 3 (Principia Press, Inc. 1939).

[8] *ECONOMETRICA,* Journal of the Econometric Society, Vol. 1, July 1933, pp. 309-24.

[9] *Id.* at p. 315.

[10] Barbour, "An Analysis of the Conclusions of the Cowles Studies with Respect to the Dow Theory," *THE ANALYSTS JOURNAL,* Vol. 4, Fourth Quarter 1948, pp. 11-20.

[11] Alfred Cowles III, "Stock Market Forecasting," Cowles Commission Papers, New Series, No. 6, 1944, p. 206.

[12] *Id.* at p. 210.

[13] Barbour, note 10 supra, p. 11.

[14] Perry P. Greiner & Hale C. Whitcomb, *THE DOW THEORY AND THE SEVENTY-YEAR FORECAST RECORD* (Investors Intelligence, Inc. 1969).

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Cyclic Analysis

A Dynamic New Approach To Technical Analysis

James Hurst

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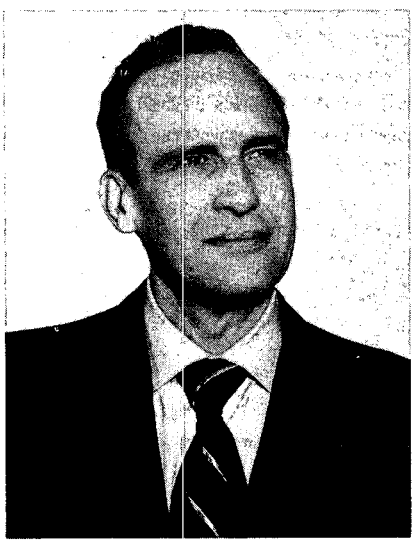
The corporation concept has been in existence since the 1300's—and negotiable equities on the North American Continent date from the issuance of Hudson Bay Company stock in about 1670. Despite this long history, it wasn't until after the turn of the last century that serious thought was given to why equity prices vary, and in what manner. At about that time several important events took place:

1889. *THE WALL STREET JOURNAL* came into existence, and with it, a wealth of accurate and readily available information on price movements as a function of time.

1896. The Dow Jones Averages were created and published. This provided graphic visibility to the form of price change versus time.

1900. Louis Bachelier wrote his provocative and scholarly paper "Theory of Speculation" that became the basis for the random-walk theory of price variation.[1]



James M. Hurst was educated at Kansas State, Brown, and Washington Universities, majoring in physics and mathematics. Following World War II, Mr. Hurst specialized for 25 years in electronics systems design for aerospace applications. In 1969, Mr. Hurst founded Decision Models, Inc. for the purpose of further developing decision theory and wave concepts as applied to the equity markets. The CycliTec aids to cyclic analysis of equities resulted and were initially published in 1971. A complete training course in these methods followed in 1973.

1902. S. A. Nelson compiled Charles Dow's ideas in *THE ABC OF STOCK SPECULATION.*[2]

Thus, within this brief span of time, documented price data became available, the random-walk theory was proposed, and one of the first technical approaches to stock market trading and investment was born.

In the following years, market enthusiasts split into three distinct groups:

1. *Fundamentalists,* holding that price movements principally reflect changes in the circumstances related to a company and its products or activities.
2. *Academicians,* unable to improve significantly on the Bachelier premise that price movements are random within reflecting bounds.
3. *Technicians,* finding particular, frequently recurring, price patterns in the past to be the harbingers of prices to come.

None of these three viewpoints really comes to grips with the problem of making money consistently in the stock and commodity markets. The random-walk theory discourages all hope of capitalizing on price fluctuations. Fundamentalists must similarly ignore the immense profit potential of price oscillations. Furthermore, the occurrence of fundamental "forcing" events is found to be nearly as unpredictable as price change is held to be by the random-walk theory. Classical technical analysis has demonstrated serious deficiencies. While the frequent appearance of empirically defined price patterns is a definite fact, applications have suffered from lack of a coherent theory on which to base methodology. Furthermore, none of the existing approaches provides a basis for a self-contained, logical, and complete solution to the money-management problems of issue selection, transaction timing, and transaction yield optimization.

Fortunately, recent years have seen the birth of a fourth viewpoint in which such capabilities are inherent. This viewpoint is based on the *Wave Theory of Price Action,* and the landmarks of development are indicated by the following events:

1938. Ralph Nelson Elliott published his well-known monograph "The Wave Principle."[3]

1940. In Pittsburgh, The Foundation for the Study of Cycles was formed.

1958. The Society for the Investigation of Recurring Events was organized in New York.

1960. The author initiated a study of the way in which human decisions are made. Equity price data was chosen for this study on the assumption that price changes reflect human decision processes. Unexpected results were obtained in the course of computerized analyses of this data. It was found that price movement can be described as a complex combination of periodic functions with specific interrelationships. This work has continued to the present, resulting in a *Theory of Irrational Decision Processes.*

1971. An outgrowth of the Theory of Irrational Decision Processes was the Wave Theory of Price Action. A book was published by the author describing practical applications of Wave Theory to the timing of stock market transactions.[4]

1971. Computerized aids to Wave Theory analysis of stock and commodity price histories became available for public use.[5]

1973. The first complete description of wave concepts as applied to the capital management problem was published.[6]

The common element between these and other related events was the mounting evidence independently offered by hundreds of researchers that a remarkable degree of periodicity characterizes time-series data describing a wide range of real-world situations—among these, the price movement of auction-market equities.

In the last decade several facts have emerged as outstanding:

1. There is very little of the random in the price movement of negotiable equities.
2. Fundamental considerations do enter the picture, but in a quite unexpected way.
3. The price movement of negotiable

equities consists almost entirely of a complex combination of wave motions with many of the predictive implications of simple wave functions.

4. The same wave functions and characteristics discovered in equity prices are found to be operative in many other situations as well.

Thus, 70 years after the events which first made it possible to question whether or not a governing law exists behind the apparently aimless meanderings of equity prices, some of the answers are beginning to emerge. Even more important, the art that has been called *technical analysis* has now become far less an art and much more a science. Methods of making use of the predictive capability implicit in the developing Wave Theory of Price Action are presently in existence and in use—and prediction of future equity price movement, however imperfect, is the name-of-the-game in trading and investing.

The remainder of this article will describe in brief the methods now being employed for making use of the Wave Theory of Price Action.

AN EVOLVING NATURAL LAW

In the last 10 years it has become increasingly evident that the widespread periodicity observed in many kinds of data implies a common cause, or forcing function. Such universal and common forcing functions are usually ascribed to a law of nature. In this instance, the emerging natural law can be stated as follows:

Numerous real-world situations, including the price behaviour of negotiable equities, reflect a common, complex, periodic forcing function. Change in the affected situations is describable as the sum of many simple wave functions. The particular waves composing the sum are a specific, describable subset in the infinity of possible such subsets. The relationships between wave variables are reasonably constant and are common to all of the situations involved.

The commonality feature implied in this law is remarkable and quite general. The same wave functions and wave-variable relationships are found to be operating in the price movement of all stocks, commodities, bonds, warrants, rights, etc.—whether traded on the New York, Tokyo, London, or other exchanges, and without regard for the time period considered. Even more remarkable, all or a portion of the same specific wave subset is dominant in the time variations of weather data, grasshopper abundance, tree ring formations, lynx procreation, bacteria division rates, and the catch of fisheries, to name only a few of the reported examples.

This natural law, as applied to explain the price movement of negotiable equities, is the Wave Theory of Price Action mentioned in the preceding section. Methodology developed to apply this theory to trading and investment problems is called *Cyclic Analysis.*

WAVE FUNCTIONS AND RELATIONSHIPS IN PRICE MOVEMENT

The Wave Theory of Price Action is embodied in a set of eight Basic Principles of Cyclicality as described in reference 6. The most significant relationships involved have to do with *waves,* the elemental building blocks of periodic processes.

An ideal wave (shown in Figure 1) varies smoothly and uniformly about a value of zero, alternately assuming positive and negative values. One complete repetition of a wave is called a *cycle.*

Only three parameters are required to completely characterize a wave (see Figure 1):

1. *Period,* the length of time elapsed from trough to trough
2. *Amplitude,* the size of the wave from trough to crest
3. *Phase,* the time position of the wave with respect to any given reference time.

In Figure 1 the phase parameter has been transformed to the more useful quantity *phase difference,* which is a measure of the relative position in time of one wave with respect to another.

The most important wave characteristic is periodicity. As one cycle of a wave is completed, another identical cycle is commenced. It is readily apparent that once the three basic parameters of a wave are known, the value of the wave can then be ascertained for all possible values of time *—including the future.* It is this ingredient of the Wave Theory of Price Action that implies predictability of future price movement.

The Principles of Cyclicality state that the price movements of all negotiable equities consist of the sum of the same set of waves with the same interconnecting relationships between the wave variables (period, amplitude, and phase). Thus, price history differences among equities are due solely to minor variations in the values of these wave variables at any given time, with the minor variations in wave variables causing large variations in the sum due to the large number of waves involved.

There is no known limit to the number of waves in the set that combine to form equity price movement. Some of these waves have periods measured in minutes, while others require many years to complete one cycle. Fortunately, it is not necessary to identify and sum all such waves in order to make use of the phenomena. Only a rather small number of waves is needed to permit useful conclusions to be drawn regarding the probable future course of equity prices. Thus, the potentially vast complexities of the Wave Theory of Price Action are reduced to the relatively simple effects and characteristics of a finite set of waves. The resulting simplified model is then used as the basis for Cyclic Analysis.

Price waves exhibit a series of extremely significant interrelationships that are identified in the Principles of Cyclicality. The most important of these are as follows:

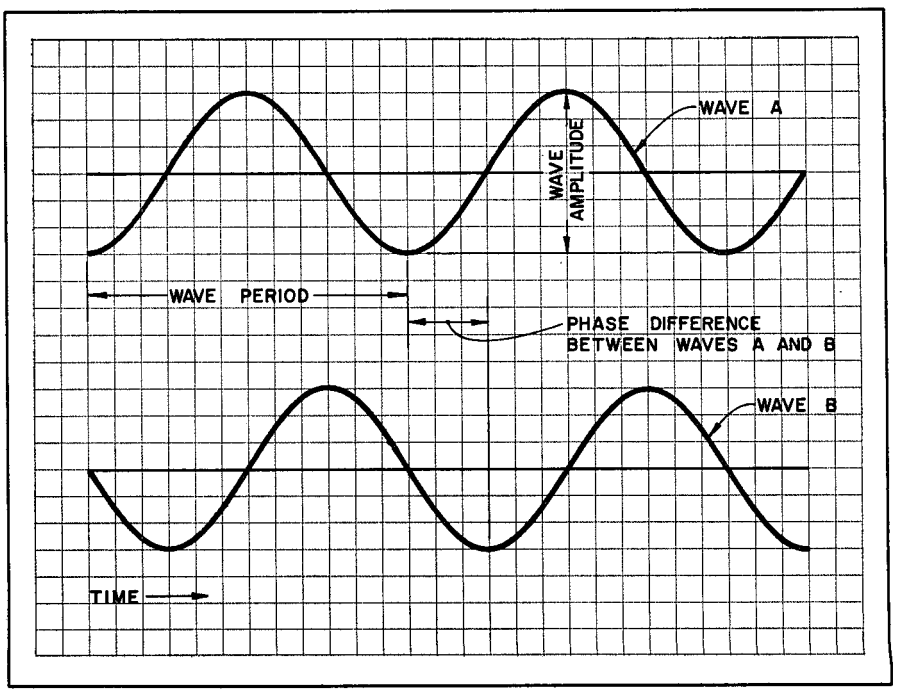


Figure 1. Basic Price Waves

1. The periods of the component waves vary about, but remain close to, a particular subset in the infinity of possible subsets of periods. This relationship is referred to as *nominality.*
2. The ratio of the average periods of contiguous waves in the nominal wave set is a small, whole number, usually two. This is known as the property of *harmonicity.*
3. The amplitudes of waves in the nominal set are approximately in proportion to the wave periods. This is the property of *proportionality.*
4. The waves in the set are so phased as to cause wave troughs to occur simultaneously whenever consistent with harmonicity. This property is referred to as *synchronicity.*
5. Total price action consists of the algebraic sum of all waves operating in a given equity at a given time. This is a statement of the linear wave combination property and is spoken of as the *summation* effect.
6. An additional relationship, known as the property of *variation,* will be dealt with in the next section.

These not-to-be-expected, but highly useful, wave relationships are responsible for most of the characteristics of equity price movement—including the recurring pattern phenomena of most classical charting methods. The implications are enormous, and the whole of Cyclic Analysis is founded on these premises.

The nominal wave periods referred to in relationship 1 are further simplified for ease of remembering to a nearly harmonic set as follows:

WAVE PERIODS

Years	Months	Weeks	Days
18			
9			
	54		
	18		
		40	
		20	
			80
			40
			20
			10
			5

This set of wave periods is spoken of as the *nominal cyclic model.* It should be noted that an important exception to the period ratio of two occurs in the case of the 18- and 54-month waves, the periods of which are related by a factor of three.

The property of proportionality implies that the amplitude of the nominal 10-day wave is twice that of the 5-day wave, etc.—but that the amplitude of the 54-month wave is three times that of the 18-month wave.

The properties of synchronicity and harmonicity lead to the expectation that at the time of a trough of any given wave, a trough will also occur for each wave of shorter period. Thus, wave troughs tend to form in groups called *nests-of-lows.* The converse is true at wave crests in that synchronicity and harmonicity preclude time groupings of wave crests. This effect is responsible for the narrow, sharp bottoms and the rounded, oscillatory tops that characterize equity price movement.

The phenomenon is illustrated in Figure 2, where a set of three ideal, synchronous, harmonic, proportional waves are summed to produce a simple composite wave representative of price movement. The diamonds below the composite wave show the time locations of the troughs of waves A, B, and C and of the resultant nests-of-lows. The triangles above the composite wave are located at the time positions of the crests of waves A, B, and C and show how wave crests fail to occur in groups. The composite wave itself shows the characteristic sharp bottoms and rounded, oscillatory top found in actual price movement.

THE INTERACTION BETWEEN WAVES AND FUNDAMENTAL EVENTS

The description given so far of price motion as a function of waves is ultra simplistic. The complexities encountered in assembling a useful model of price change can, however, be conveniently grouped under the heading of *wave modulation.*

When three or more ideal waves having certain specified interrelationships are summed (the periods are not harmonically related, but are rather close together), a special modification of a single ideal wave is produced. Such a modified wave is said to be *modulated.* A modulated wave retains most of the predictive advantages of an ideal wave, but amplitude and period fluctuate slowly as time passes.

In actual price movement, it is found that the waves in the nominal cyclic model are not single ideal waves at all. Instead, each wave is made up of a bundle of closely spaced waves that sum to form a modulated wave. The average periods of these modulated waves correspond with those given in the nominal cyclic model. The fluctuations in the period and amplitude of these modulated waves are referred to as the property of *variation.*

This property of price waves is then further complicated by the effect of fundamental events. The impact of news releases, earnings expectations, product development, and the like is wholly absorbed as an orderly *amplitude change* in a contiguous-period subset of the nominal cyclic model. The result is additional modulation of the basic price waves. The extent of fundamentally induced amplitude variation and the number of waves affected depends on the nature of the fundamental event and on the degree to which this event alters volume interest in the equity.

The all-important result of this behavior is that fundamental events do not disturb the *periods* or *phases* of price waves—and therefore do not disturb price movement *timing* predictions. Instead, the wave amplitude changes involved cause a change in price volatility. If a fundamental event has a high impact or is persistent, waves with relatively long periods will undergo amplitude changes. When this happens, the equity price will exhibit a relatively long lasting rise or fall (depending on the nature of the fundamental event) upon which the oscillations of the shorter waves are superimposed. These fairly common long lasting rises or falls are termed *pseudo trends* and may persist for weeks, months, or even years. They are produced entirely by the normal summing of waves in the cyclic model, but the longer waves in the model have undergone amplitude changes as a result of a fundamental event.

From a theoretical standpoint, the interaction of fundamentals with cyclicality can be considered to be a part of the modulation effect already present.

In light of this curious behavior of price waves in response to fundamental events, several previously puzzling aspects of price movement can be explained:

1. Cyclic predictions, such as the price reversals at nests-of-lows, are made entirely on the basis of past price history. Yet, invariably, when these predictions come to pass, a suitable fundamental event is present to "account" for the resulting price response.

If the subsequent price movement is

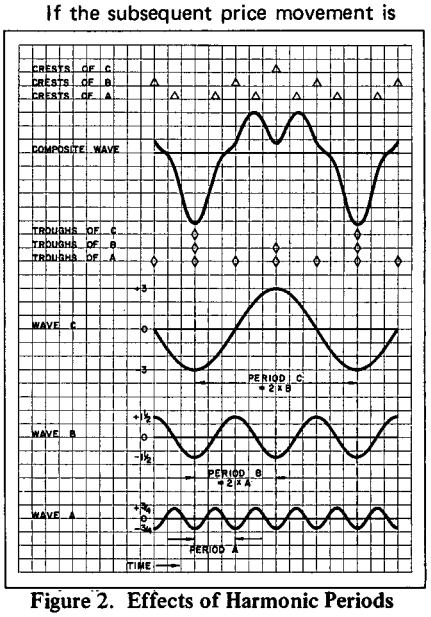


Figure 2. Effects of Harmonic Periods and Synchronized Wave Troughs

in accordance with the usual expectations for a cyclic model with normal wave amplitudes, then it is likely that the fundamental event cited as "causing" the price reversal was merely the one event, among the many events that are always available, that was selected by the analyst as best fitting the circumstances under consideration.

If the subsequent price movement exhibits a pseudo trend, either short-term or long-term, then it is likely that a true fundamental interaction is present. Further, it is likely that the fundamental event was in synchronism with the cyclic model for equity price movement because it was brought about by the same human decision processes that produce price movement.

2. The use of Cyclic Analysis by a large number of investors does not destroy the wave behaviour of price movement.

Such use constitutes an alteration in volume interest, which is the intermediate result of *any* fundamental event. Thus, the effect on price waves is identical to that produced by any other fundamental event; namely, amplitude increase in a subset of waves resulting in volatility change, but no change in price-reversal timing.

3. Fundamental events such as the activities of Federal agencies in regulating money supply can be shown to correlate with price behavior around 54-month price lows and highs. Yet such 54-month waves have been present in price movement throughout market history, including the time before these agencies existed.

This observation is subject to the same explanatory comment as item 1 and serves to emphasize the point.

It is this very important relationship between fundamental events and price wave amplitudes that makes possible a wholly technical basis for forming stock and commodity transaction decisions.

PREDICTING PRICE REVERSAL TIMING

Wave Theory permits precise definitions of such concepts as *trend* and *trading cycle* to be derived. Quantitative definitions of this sort are significant benefits of great practical utility. Nevertheless, these accomplishments are minor by comparison with Wave Theory's ability to estimate price reversal timing *in the future.*

It is clear that practical use of wave concepts is dependent on the ability to separate individual wave components from past price data and to estimate the periods and phases of these waves. The Cyclic Analysis process used to accomplish these aims is called *formal phasing analysis,* or *FPA.* The methods employed in conducting an FPA are predominantly graphical and include the use of computer generated aids.[5] These methods are described in detail in reference 6.

An FPA results in the identification of the time position of each trough of each wave of the cyclic model active in a given issue at the time of the analysis. From this information the average period and the phase of each wave are obtained.

The average wave period and the period variation experienced in the past are then extrapolated from the latest identified wave trough, repeatedly, until the trough timing for each wave of interest is estimated for any desired portion of future time. In this way, estimated time positions (with tolerance limits) for future nests-of-lows are established.

Powerful assistance in the process of wave trough location is provided by the properties of nominality, harmonicity, and synchronicity through the following considerations:

1. The resulting wave period estimates must fall within a known range of the nominal model wave periods.
2. The known harmonic relationships between contiguous wave periods must not be violated.
3. The estimated future time positions of successive wave troughs must continue the synchronized pattern of trough locations established in past time.

Price reversals in the upward direction are then expected to take place at the estimated times established for future nests-of-lows—within the tolerance range determined in the FPA. The number of wave troughs involved in a nest-of-lows provides an immediate indication of the potential strength of the reversal.

Price reversals in the downward direction are predicted by establishing the estimated time positions of future wave crests. Since these crests are not synchronized, the actual component wave whose crest is most likely to be associated with the price high is determined from predictions of future trend and the resulting time translation of price high relative to wave crest.

From the foregoing, it can be seen that Wave Theory provides a way to estimate in a logical fashion the future time of occurrence of price reversals that will be followed by price moves of any desired magnitude in either direction. The Cyclic Analysis methodology used in the prediction of price-reversal timing is demonstrated in Figure 3. This is a typical graphic display of the kind in use for the analysis of stocks and commodities.[5] The price and time grid lines normally present have been removed for the sake of clarity in reproduction.

An FPA has been performed and the wave trough locations are indicated by diamonds below the price bars. The Periodogram at the bottom of the chart is computer-generated and provides estimates of the wave components active in this particular equity at the time of the analysis. This Periodogram and the smooth envelope enclosing the price bars are the primary computer-generated tools used in carrying out the FPA. The average wave periods resulting from the FPA are shown to the far right of the associated rows of diamonds, and several of the extrapolated future time positions of nests-of-lows are indicated. The expectation demonstrated is for a price reversal in the upward direction to occur in approximately two to three weeks, powered by the reversal of all waves up to and including the nominal 18-month wave.

The tabulation shown on the chart is known as a *current cyclic model* and is a compact way of organizing the information gained from an FPA. In this table, the periods of the nominal cyclic model are shown to the left for comparison with the actual FPA average periods obtained. Wave phase is tabulated in terms of time elapsed since the last identified wave trough. The arrows shown are developed from phase status and show the current direction of action of each wave. The columns at the far right contain numbers derived from average wave periods which permit construction of graphic devices for price-move prediction.

Figure 4 shows the same equity at a later time with the price-reversal timing predictions from Figure 3 overlaid for comparison. It is seen that the predicted timing was very close indeed and that the reversal resulted in a price move from 32 to the 60's. Except for predictable minor oscillations, prices subsequently moved uninterruptedly to the region of 90 before the effects of this powerful nest-of-lows subsided.

A COMPLETE TRADING SYSTEM

A fully integrated trading system must have the following characteristics and capabilities:

1. Permit preplanned investment goals
2. Supply issue selection criteria
3. Permit pretransaction evaluation and comparison for transaction selection purposes
4. Provide for automatically triggering transaction entry
5. Provide for intratransaction analysis for the purpose of optimizing transaction termination.

As these capabilities are discussed individually in the following paragraphs, it will be seen that the preplanning of investment goals is closely tied in with several of the other capabilities of the

system.

Issue selection is a particularly simple proposition in the application of Cyclic Analysis. Since the approach is wholly technical, the industry represented, the products supplied, and other fundamental considerations are incidental. The equity is considered only as a set of price-time data against which Cyclic Analysis procedures are to be applied. In practice, a set of several equities is maintained in an analyzed condition. Such a set is called a *stable.* Criteria for stable selection include corporate stability, price volatility, equity fluidity, and sufficient uninterrupted data to permit computerized analysis operations. These elements are judged with investment goals in mind.

Pretransaction evaluation is a direct fallout of the Wave Theory analytical processes discussed in previous sections. To develop this point, the following definitions are needed:

1. *Transaction risk:* the probability that any single transaction will result in a capital loss instead of a capital gain.
2. *Risk potential* or *risk:* the amount of capital that may be lost if the transaction fails.
3. *Profit potential* or *potential:* the amount of capital that will be gained if the transaction succeeds.
4. *Percentage potential:* potential expressed as a percentage of invested capital.
5. *Potential-risk ratio* or *PR ratio:* the ratio of potential to risk.

In practice, investment goals are preset in terms of these parameters. For example, transaction risk should be set at 0.5 or less. The PR ratio should be set at 3.0 or more. And the percentage potential should be set at 20 percent or more.

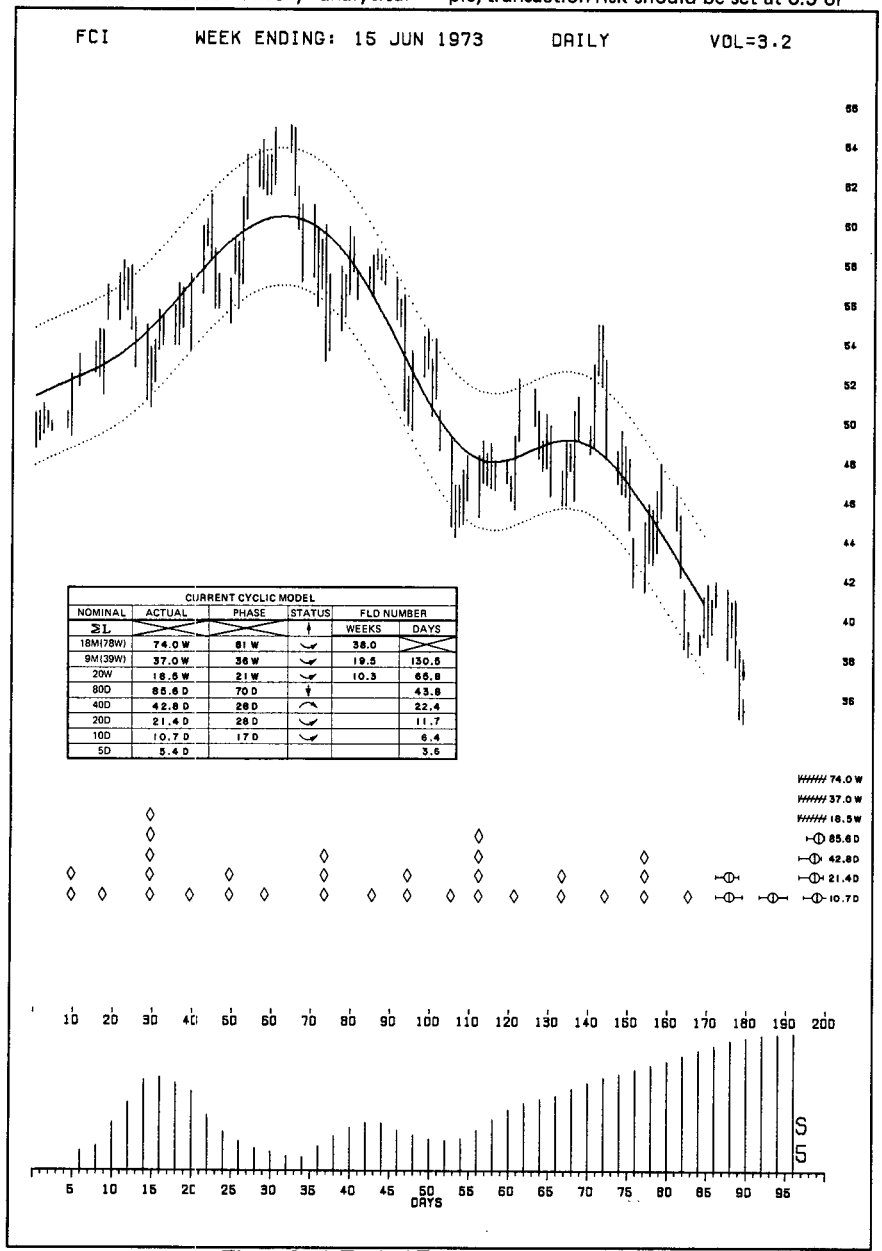


Figure 3. A Typical Formal Phasing Analysis

To illustrate, let us suppose that Cyclic Analysis has identified an upcoming possible long transaction by the usual means of trading cycle potential evaluation and FPA prediction of price-reversal timing. Assume that further analysis[6] predicts a price move to 31 from an expected transaction entry price of about 19. A predicted price objective for the trading cycle low at the upcoming reversal leads to the expectation that the stop-loss level can be set at about 17.

Simple relationships connect these transaction variables as follows:

$$B = \frac{(PR \times SL + S}{PR + 1}$$

$$\% = \frac{100 \times (S - B)}{B}$$

Where B = Buy price
PR = Potential-risk ratio
SL = Stop-loss price
S = Sell price
% = Percentage potential

Similar relationships are available for short transactions and for margined and commodity trades.

In the example cited, these relationships would be used to produce the following tabulation:

EVALUATION OF
LONG TRANSACTION

Sell 31 Stop Loss 17

Buy	PR	% Gross
21.67	2	43.05
20.50	3	51.22
19.80	4	56.57
19.33	5	60.37
19.00	6	63.16
18.75	7	65.33
18.56	8	67.03
18.40	9	68.48
18.27	10	69.68

From this tabulation we can arrive at the following conclusions:

1. A buy at the price of 19 would result in a PR ratio of 6.0 and a percentage potential of 63.16 percent, both quite acceptable.
2. The maximum acceptable buy price is 20.5 because that price would result in the minimum acceptable PR ratio of 3.0. The resulting percentage potential would be 51.22, also acceptable.

The following points should be noted: this evaluation is produced prior to the

price reversal on which the planned transaction is based; this evaluation can be compared with those of other potential transactions in order to select the transaction that is most advantageous; and any desired investment goals can be implemented at will by simply changing the acceptable parameter values. Thus, the ability to conduct transaction selection on a quantitative comparative basis has been achieved—along with the preplanning of investment goals.

Cyclic Analysis provides the action signals (known as VTL's and FLD's[6]) needed to prevent errors in wave assumptions from increasing transaction risk to unacceptable levels. Once an action signal is selected, equity price movement is tracked to determine the exact transaction entry time, or preset orders are issued to the broker.

Once a transaction is entered, it is continuously monitored by means of intratransaction Cyclic Analysis. Wave and price events are predicted, and actual events are compared with these predictions to determine the *transaction progress situation.*

There are three transaction progress situations: on track, better than expected, and worse than expected. Each transaction progress situation is associated with definitive modes of transaction termination in such a way as to minimize losses and maximize gains.

If the transaction is classified as either better than expected or worse than expected, then a change in the mode of transaction termination is called for. It may also be necessary to modify the wave assumptions on which the transaction was based. The nature of these modifications influences the selection of the new mode of transaction termination.

It should be realized that the operation of a trading system such as the one described here produces a net yield based on the results of a *series* of transactions. For example, suppose that average transaction risk for a number of transactions taking place during a year's time is as low as 0.5—meaning that as many losses are incurred as gains. Such an operation can still be immensely profitable if the PR ratios average 3.0 or better, since the average gain is then three times the average loss. Cyclic Analysis has the potential of achieving transaction risks on the order of 0.2 or 0.3, with correspondingly increased profitability.

CONCLUSION

The steadily accumulating and increasingly convincing evidence of the cyclic character of many natural and man-made phenomena provides a fascinating field for study and research. One result of such research, the Wave Theory of Price Action, grew out of an investigation of man's decision making processes. Continuing research may eventually uncover a common causative factor behind this and other similar, but seemingly causatively unrelated, phenomena.

In the area of the practical application of this new cyclic knowledge, there is little question that continuing research will lead to increased understanding of the Wave Theory of Price Action. Also, the applications, methods and techniques embodied in Cyclic Analysis will undoubtedly be improved, particularly in the area of computer-generated aids.

In the meantime, the present state of the art has proven extremely useful. Cyclic Analysis methods have been in the field since December 1971. The techniques involved are documented in detail in reference 6, and the computerized analysis aids described here are available as reference 5. ◻

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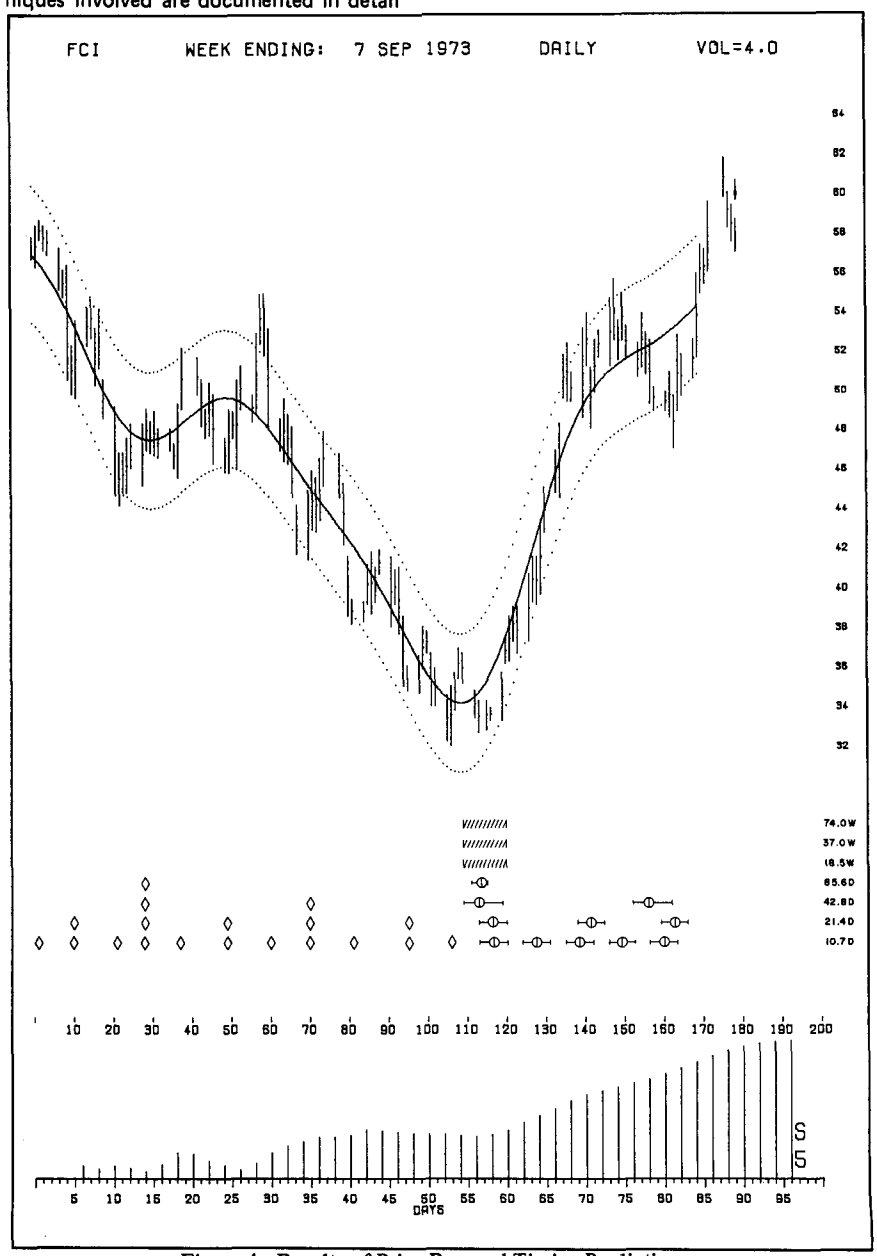

Figure 4. Results of Price Reversal Timing Prediction

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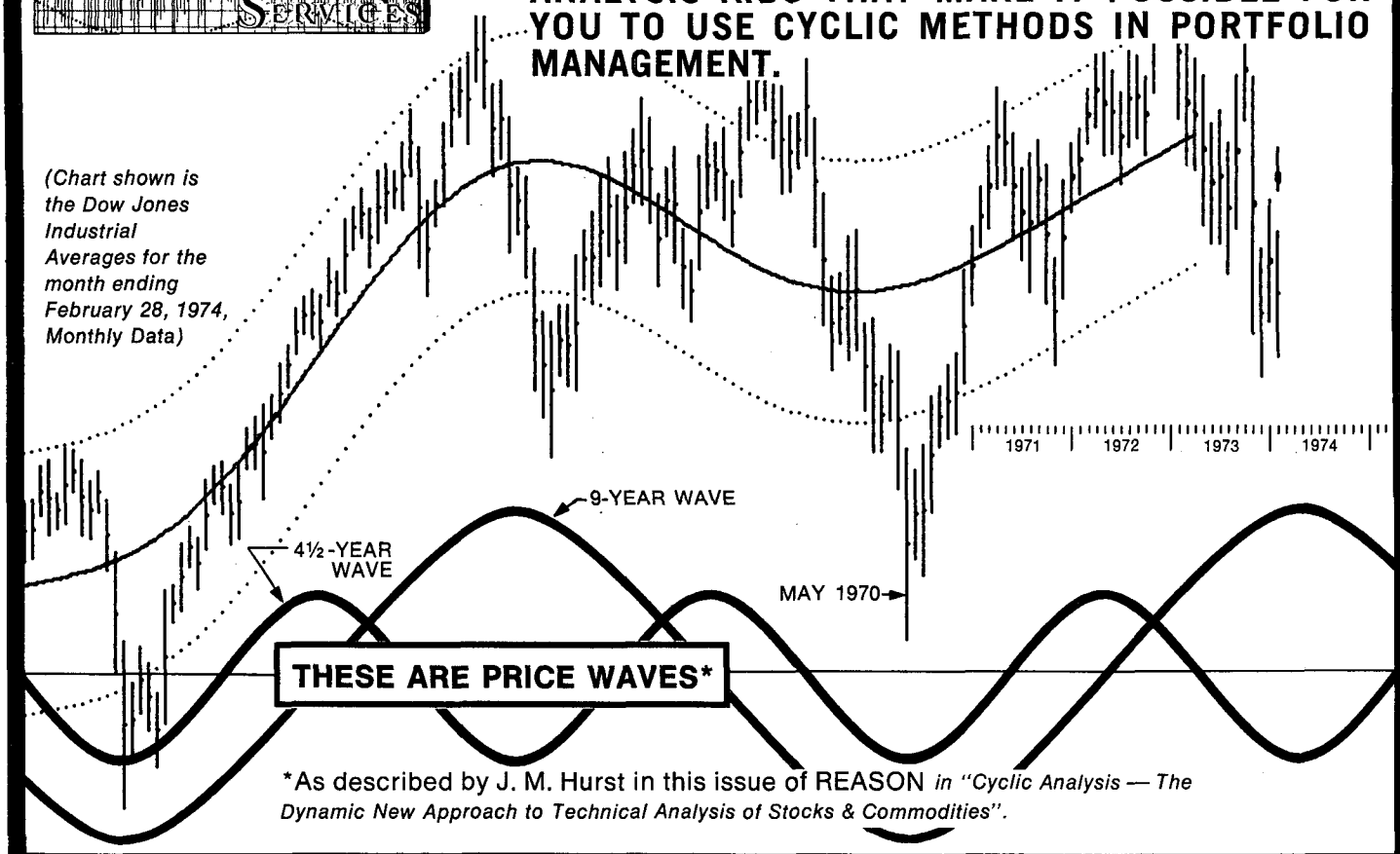

*As described by J. M. Hurst in this issue of REASON *in "Cyclic Analysis — The Dynamic New Approach to Technical Analysis of Stocks & Commodities".*

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THE COMING COLLAPSE IN REAL ESTATE

Edmund Contoski

Major economic contractions all have the same cause: government manipulation of the country's money and credit. An economic contraction, that is, a recession or depression, is a correction of economic distortions that have built up during the preceding government expansion of credit. Various factors, mostly resulting from government policies, cause this credit to expand more easily in some segments of the economy than in others. Of course, any major inflation quickly affects all aspects of the economy, and all feel the subsequent effects of the ensuing deflation. But those segments of the economy into which inflated credit flowed most easily are the ones where the subsequent correction will be most dramatic.

The 1929 crash, while it affected all segments of the economy, was most dramatic in the stock market because it had become the primary outlet for the excess credit generated by the Federal Reserve in the preceding years. In other economic crises in our history the most striking collapse has occurred variously in commodities, land, the banking system, or some other area, depending on the credit structure of the time. While these crises have been repeated at almost regular intervals throughout our history, as a rule the collapse has not hit hardest in the same field twice in a row. This may be partly because the most recent cycle is within the memory of more people, leading them to be more cautious in that field. Most people expect the next economic crunch to be like the last one. In reality it is *least* likely to be like the last one. This is not only because of people's caution but because government policies in a mixed economy cause credit to flow unevenly through the system, and these policies are changed after every boom-and-bust cycle. So the next time the government resorts to inflation, the collapse comes in a different area.

Edmund Contoski has held various positions with several land development/home building companies and urban consulting firms, including: Director of Planning and Development, The Kennedy Company; Director of Planning, E. A. Hickok & Associates; Planning and Research Manager, Unimod Division, Pemtom, Inc.; and Senior Planner, Nason, Law, Wehrman & Knight, Inc. Mr. Contoski is also the author of the book THE MANIFESTO OF INDIVIDUALISM.

WHERE THE COLLAPSE WILL COME

For the above reasons I do not believe the stock market will be the primary recipient of deflationary forces as it was in 1929. Make no mistake about it: I expect stock prices to tumble, as they already have begun doing. I simply expect the collapse in real estate prices to be much worse.

After 1929 the government restricted the margin buying of stocks, never again allowing stocks to be purchased on such thin margins. Despite the government's concern for restraining credit for stock purchases, over the last 40 years the government has progressively made it easier to obtain credit to buy a home. In the 1970's it has been common to purchase homes with down payments as low as 10 percent and possible to do it at 5 percent—which was not the case in 1929.

The whole credit structure of the real estate market as we know it today did not exist in 1929. That in itself is one of the reasons it has escaped the scrutiny and concern that has been focused on the stock market. The present structure of the real estate market has never been subjected to the strains the stock market has seen; it hasn't been around long enough. It's one of those areas where the government policies were changed after the last cyclical bust.

The present inflated values of real estate are the result of: (1) the government's monetary policy, tax policies, and financial regulations, (2) various federal

grants, programs and social legislation, and (3) the suburbanization movement. The first two categories are obviously within the scope of government action, but the ways in which the government contributed to the suburbanization movement are not generally recognized. It is important to understand the suburbanization trend of recent decades because that is where the action has been; it's where most of the real estate money has gone, where most of the building has taken place—and where land prices have skyrocketed. Suburbanization, while not totally the product of government action, was strongly stimulated by it in many ways.

"Most people expect the next economic crunch to be like the last one. In reality, it is least *likely to be like the last one."*

Like the inflation of the dollar, the government's influence on the rush to the suburbs began during the Roosevelt administration, thanks to the New Deal thinkers who were responsible for so much radical legislation in that era.

In 1931 Herbert Hoover called a national conference on housing. The conference made various recommendations for increased federal action, but nothing was done. The Roosevelt administration used some of these recommendations, coupled them with still more radical ideas of its own, and enacted them into law along with a flurry of other social legislation. The Home Owners Loan Act, the National Industrial Recovery Act (resulting in the National Planning Board and the Public Works Emergency Housing Corp.), the National Housing Act of 1934 (which established the FHA), and the Housing Act of 1937 were some of the laws enacted.

THE NEW DEAL PLANNERS

In that era the leading urban thinkers were "Decentrists," as Catherine Bauer aptly labelled them. This group included Ms. Bauer, Lewis Mumford, Clarence Stein, Henry Wright, Tracy Augur, Russell Van Nest Black, and others. They viewed the cities as failures, as evil, and believed salvation lay in getting people out of the cities and into the suburbs and small towns. This view, as with city planning ever since, was based on the earlier simplistic and unrealistic "Garden City" concept of Ebeneezer Howard. But as Jane Jacobs pointed out, "Howard was envisioning not simply a new physical environment, but a paternalistic political and economic society."[1] Thus the physical planning theories of that time fit well with the political views of the New Dealers.

Henry Wright and Clarence Stein were the designers of Radburn, N.J., a garden city-type plan modified for the auto age. Significantly, it was a suburb and was designed for only 25,000 people. Wright and Stein became members of the planning advisory group to Roosevelt's Resettlement Administration. Wright also toured the country for the National Association of Housing Officials campaigning for more public housing. Tracy Augur became a planner for TVA (another Roosevelt program), co-designed the federal town of Norris, and also was a member of the Resettlement Administration planning advisory group. The administrator of that agency, Rexford Tugwell, also had a Decentrist point of view:

> My idea is to go just outside centers of population, pick up cheap land, build a whole new community and entice people into it. Then go back into the cities and tear down whole slums and make parks of them.

Catherine Bauer authored *MODERN HOUSING*, was executive director of the Labor Housing Conference, and testified before Congress on behalf of housing legislation. Mumford was, and is, an influential critic and author of many books denouncing the city. Black helped to promote the Planning Foundation of America, was selected by the National Planning Board to serve as a consultant to several states, and was also a member of the Resettlement Administration group.

Given the orientation of the opinion makers and people in power, it is not surprising that government created a national mortgage market with tax-backed guarantees so that the common man could leave the city and own a home in the outskirts. The Housing Act of 1937 even provided federal loans for buying peripheral sites for low rent housing.

The New Deal set the direction. It firmly established housing as an issue to be dealt with by the federal government. The government stimulated and subsidized private housing and influenced the flow of private credit in real estate. The government got directly into the real estate market in public housing projects, as a land developer, and a builder of whole new communities. The government established—indeed helped to create—the American ideal of a single-family home in the suburbs. In this it found something that the modern populace wanted even more than "bread and circuses," which the Roman government provided to keep *its* citizens content.

Politicians ever since Roosevelt have been practically stumbling over each other to try to deliver more of this American ideal to the public. Politicians could perpetuate themselves in office by buying votes with the taxpayers' money as long as the money was spent to please the voters. Thus, for example, when Harry Truman was reelected in 1948 after a campaign of blasting "that notorious do-nothing Republican Eightieth Congress," even conservative senators such as Robert Taft and William Knowland introduced a housing bill to counter a similar bill presented by the Democrats. The resulting bill with bipartisan support became the Housing Act of 1949, the most comprehensive bill of its kind up to that time. It provided a billion dollars for loans, $500 million for capital grants for redevelopment, and authorized 810,000 new public housing units.

"The New Deal firmly established housing as an issue to be dealt with by the federal government."

STIMULATING THE SUBURBS

For 40 years the government has steadily expanded its role in housing and urban development by passing new bills, broadening its own powers, appropriating more funds, expanding the coverage of its programs—and adding more employees. Always adding more employees. And constantly adding impetus to the suburbanization movement. For example, it has always been easier to obtain FHA approval in the suburbs than in the cities. Government policies have consistently encouraged home ownership. In addition to furnishing mortgage guarantees, the government provides a further incentive by allowing interest on home mortgage payments as a deduction on federal income tax. Local governments also discriminate

in favor of home owners by allowing homestead exemptions on property taxes. All these have contributed to the boom in home building in the suburbs. Anything encouraging the single-family home was bound to result in significant suburban development since single-family homes take up larger land areas than higher density housing types.

There were other ways, too, in which the government abetted suburban development. Billions of dollars were appropriated for federal highways, which made the suburbs more accessible, and for sewer and water grants, which gave the suburbs utility systems comparable to the big cities. Since the suburban residents paid for only a portion of these costs, they were receiving benefits subsidized by other taxpayers.

The financial effect of all the stimulants to suburban growth was to escalate prices, aside from the inflationary pressures that were raising prices everywhere. The latter merely added to the former, making the price rise seem even more spectacular. The supply of suburban land was limited, and the many financial incentives to suburban development exaggerated demand.

REGULATING INVESTMENT

Over the years increasing government funds have been spent on urban renewal, low-income housing, housing for the elderly, and various other programs involving or affecting real estate. The greatest effect, however, has not come from public funds or public construction but from the way in which the government has influenced private capital and private construction. The effect of the Interstate Highway System on private construction is an example of a public project having tremendous effect on the pattern of private development. It is possible, however, for the government to effect consequences of great magnitude without any public project at all simply by the government's regulatory powers over financial institutions.

The most important source of credit for real estate development is the private institutions. Of these the largest, in terms of mortgage holding, are the savings and loan associations, followed by the life insurance companies. For decades the S&L's have been allowed by the government to pay higher interest on savings than the banks. This gave the S&L's a competitive edge in bidding for savers' dollars and channeled billions of these dollars into real estate. The government prevents the S&L's from investing in anything but real estate!

Earlier it was pointed out that the government has diverted money into real estate by tax incentives for home owners, but these are not the only tax provisions which favor real estate. The depreciation and capital gains features of the federal income tax have attracted huge investments in real estate. Many a real estate development would not make economic sense, and would not have been undertaken, except for the depreciation schedule. Many a parcel of land has been bought as a tax shelter.

DESTROYING THE CITIES

To this point we have discussed ways in which the government has supplied positive incentives to the real estate boom. This boom has also received impetus from negative or contrary stimuli, as a reaction *against* certain policies and problems. For example, the failure of governments at all levels to deal effectively with riots and crime in the cities, the massive failures of urban renewal, the corruption of many big city governments, the problems of integrating schools, and similar social issues have all resulted in more people moving to the suburbs.

Another contrary stimulus has been government monetary policy. In proportion as the government has resorted to inflation, real estate has attracted more money—and not just because there are more dollars available. The greater the inflation, the more incentive there is for people to own their own home or other property. (The boom in condominiums is largely a result of this.) Real estate has increasingly become a substitute for a monetary function. One of the essential functions of money is to serve as a store of value. Unhappily the dollar no longer does this. As people lose confidence in deteriorating paper, anything of tangible value becomes more desirable. Real estate has a particular attraction in this regard because:

1. The amount of land is fixed.
2. Income-producing real estate generally offers a better return than common stocks and a hope for appreciation that higher-yielding fixed-return instruments do not have.
3. The real estate market does not fluctuate daily the way commodities and stocks do. This relative stability is the result of a thin market for any given property. Sometimes a piece of property will be on the market for many months or even years before finding a buyer, whereas shares of stock in any medium-sized company are traded every day. This slowness of the real estate market allows it to avoid the minor dips evident in stocks and commodities and gives real estate an image of solidarity.
4. The history of suburban development leads to extravagant hopes for property appreciation in the future.

Fears of inflation have affected the investment policies of the big institutions as well as those of individuals. The institutions found themselves in the difficult position of supplying long-term mortgages at fixed rates of return while inflation continued to mount. This led to demands for "a piece of the action"—some form of participation in development projects. It also led to the purchase of huge tracts of raw land beyond immediate development needs as a way of "banking" assets for the future. The demand created by these institutions bid up land prices correspondingly.

The financial institutions were not alone in jumping into real estate. In the late 1960's nearly 300 major corporations, from Alcoa to Westinghouse, joined the bandwagon.

Now the trend is reversing. Institutions that were flush with money and enthusiastic about investing in real estate are in a different position today. Many of the corporate giants that eagerly entered the real estate field only a few years ago have suffered severe financial losses and are now just as eager to leave the field. Some already have. Here are some of the larger real estate losses: Boise Cascade $257 million, International Paper $30.5 million, International Telephone and Telegraph $57 million, Westinghouse $30 million. [2]

"The greater the inflation, the more incentive there is for people to own their own home or other property."

THE S&L SQUEEZE

In addition to the fact that many large real estate developments have not lived up to expectations, the financial institutions trimmed their plans because changes in interest rates reduced the amount of money available to them. During the past year the government changed its regulations to allow banks to offer higher rates for certificates of deposit. This plus the rates available on commercial paper and government securities caused a tremendous flow of funds away from the S&L's. Although more recently there has been a modest reflow of funds to the S&L's, it is

highly unlikely such funds will result in a credit expansion massive enough to revive the boom in real estate development. The first priority for any new funds for the S&L's will be to pay back high interest loans from the Federal Home Loan Bank, which are up sharply as a result of the last credit crunch. Furthermore, the wide fluctuations in interest rates over the last few years make it unlikely that the S&L's and other institutions will commit themselves to large-scale, long-term development projects as they were doing just a few years ago. Projects of that scope require a stable economic climate for an extended period of time, which few money managers now anticipate. Thus the demand for large land areas suitable for development is now diminished among the same institutions that helped bid up the prices. Moreover, many of the institutions that formed joint ventures of one sort or another with land development companies or home builders are finding these marriages less than happy and are not anxious to extend themselves in that direction.

Meanwhile, high interest rates are killing the homebuilding industry by raising its costs while destroying its market. The building industry operates on borrowed money, the costs of which are now greater than most companies have prepared for, leaving many in serious financial difficulties. At the same time, the high interest rates have turned off the buyers. For most people buying a home is not an immediate necessity; it is a purchase they can postpone.

Right now consumer sentiment is very negative. The highly regarded University of Michigan Consumer Sentiment Survey, as well as other public opinion polls, shows the public with an extremely pessimistic economic outlook. A home is the largest purchase most people ever make. They are reluctant to make it in an adverse economic climate.

As to the numerous statements from government and industry sources about the need for a specific number of new housing units every year, I can only say that people will find they can get along without them. In hard times people will double-up. Couples will move in with their in-laws, or perhaps take in a lone surviving parent. Youngsters now enjoying the luxury of an apartment by themselves will move back with their parents or in with each other.

"With high interest rates and a gloomy market outlook, land inventories will be viewed as liabilities to be disposed of rather than as assets."

THE BAD NEWS FOR REAL ESTATE

As the euphoria of inflationary prosperity gives way to hard economic realities, the effect of trends adverse to the past suburban development pattern will become more apparent to the real estate industry. Here are a few of these:

1. In view of the oil crisis the consumer is apt to think twice before going further and further out of the city to buy a home and increase his commuting distance.
2. The Interstate Highway System is virtually complete. It seems unlikely any new major highway programs will be initiated soon, not only because of the oil situation but because of environmental, traffic, and other considerations. In fact, pressure is developing to use highway funds for mass transit systems. This would work against the continuation of the past pattern of suburban sprawl. Efficient mass transit systems can be developed only where there are higher densities.
3. The trend in the birth rate indicates that pressures for real estate development will not continue as they have in the past. In this I do not mean merely the recent spectacular drop in the birth rate. I am referring to the fact that the famous World War II baby boom has now matured to the family formation age. New family formations, indicative of a potential housing market, will not continue the past growth rate. The abundance of empty classrooms in the schools should tell the real estate industry what to expect.
4. Due to the publicity of numerous scandals and waste connected with government housing, urban renewal, and similar programs, these programs at long last appear to be coming to an end. Even FHA is winding down. In 1971 FHA processed 369,000 applications for assistance on single-family homes. In 1972 the number was 140,000, and last year it was only 44,000.

I believe the first effect on real estate of the deflationary forces shaping up will be a drop in raw land prices. Builders will sacrifice their future land inventory in order to maintain their current operations, and institutions and investors will scrap their long-term plans for the sake of their immediate cash requirements. Also, much land is held on very thin margins. With high interest rates and a gloomy market outlook land inventories will come to be viewed as liabilities to be disposed of rather than as assets to be retained for the future. Land held for future development does not pay its current carrying costs.

The decline in land values will spread to the values of developed real estate. In addition the low margins which have been encouraged for home owners will turn out to be troublesome. Too late it will be recognized that many who bought homes because of the easy credit available simply should never have been home owners in the first place.

As unemployment rises, the home owners' difficulties in meeting mortgage payments will be paralleled by businesses facing an increasingly bleak economic outlook. Prices of commercial and industrial real estate will adjust accordingly.

In time of crisis the very factor which exempted real estate from frequent fluctuations in price and made it appear so stable will work against it. The slow market, the lack of trading activity, will make it difficult to sell property quickly when it is necessary to raise cash. When cash is needed quickly, prices will be slashed to promote sales.

In a major economic contraction most of the tax incentives in the real estate industry will diminish in importance. The tax-shelter characteristics, for example, will not be important if profitability disappears.

In retrospect it might seem to some (not libertarians) that the problems the real estate market is headed for could have been avoided, or at least reduced, by stricter regulation of the industry, notably in the area of margin requirements. But that is not the problem; it is only a *symptom* of the problem. The problem is the government's power to generate credit. Blocking or restricting the flow of credit in a given area is no substitute for sound money, which is the only way the boom-and-bust cycle can be avoided. Whenever inflationary pressure builds up in even a semifree economy, it will find an outlet. Plugging one hole through which excess funds can flow merely increases the pressure within the system, and capital will find an outlet in other directions.

WHAT TO DO?

With the prospect of a bleak future for the real estate industry, what should the individual do? Here are my rules for real estate for the next few years:

1. **Do not even think about real estate as an investment for the foreseeable future.** This means avoiding real estate investment trusts (REIT's), real estate

syndications, or individual properties for speculative or investment purposes. (Some of the REIT's have already taken a beating.) If you are convinced you must buy real estate for your own immediate needs, personal or business, then do so with the understanding that that alone justifies the purchase; do not rationalize that it also will be a good investment or will preserve your capital. It would be better not to buy at all at this time and to dispose of whatever real estate you own with the possible exception of your own home. Actually, you could probably profit by selling your home, if you own it, and buying another in a couple of years. But would the inconvenience or the change in your life style be worth the financial return? Everyone must answer that for himself. My own view is that if you have managed your other financial affairs prudently, if you own your home, or at least do not have a large debt against it and can foresee your ability to pay it, then why not treat yourself to living in the home you like? You will always need a place to live. On the other hand, if you are heavily in debt, if you have no hard money assets and your future income is questionable, sell now and rent.

2. If you are determined to own real estate in the period ahead, maintain as much financial and legal independence as possible. By this I mean avoid situations which bind you to the fortunes and decisions of other. Joint ventures, partnerships (including limited partnerships) or any other variety of multiple ownership (except joint tenancy for couples) should be avoided.

3. Make all leases for the shortest term possible. Current monetary instability renders it unwise to make long term commitments at this time. This applies to commercial and industrial properties as well as residential. I suspect future economic dislocations will also make many choice properties available.

This article has been concerned with urban and suburban real estate. Agricultural real estate has been deliberately excluded because it will be affected more by the market for agricultural products than by factors affecting urban and suburban real estate.

While recreational real estate has not been mentioned thus far, it is obviously a luxury. Such properties are in much demand in good times but not in hard times. If you are intent on buying a recreational property, look at it on the basis described under Rule One above: as a deliberate expenditure for your own needs or desires, not as an investment. If you can justify it in your own mind on that basis, go ahead; otherwise, forget it.

The only alternative I can foresee to the economic contraction predicted in this article would be a mere postponement of this inevitability by means of an intervening period of runaway inflation. The above rules should serve well in this eventuality also, for the end result would be the same only worse. Runaway inflation would surely destroy the mortgage market. New construction would grind to a virtual halt. Valuations of developed real estate would no doubt increase for a while along with everything else, but few people would profit. A small minority of exceptional properties would probably stay ahead of inflation, but the vast majority would not. In view of the illiquid nature of real estate it would be extremely difficult to ride the wave of inflationary valuations and then *exit* before the runaway inflation turned to collapse.

Real estate has been an excellent investment vehicle at many times in the past. It will be again at some time in the future—but not in the years immediately ahead. ◻

NOTES AND REFERENCES

[1] Jane Jacobs, *THE DEATH AND LIFE OF GREAT AMERICAN CITIES* (Random House 1961) Vintage book edition, p. 18.
[2] "Corporate Giants that Soured on Real Estate," *BUSINESS WEEK*, Feb. 16, 1974, p. 18.

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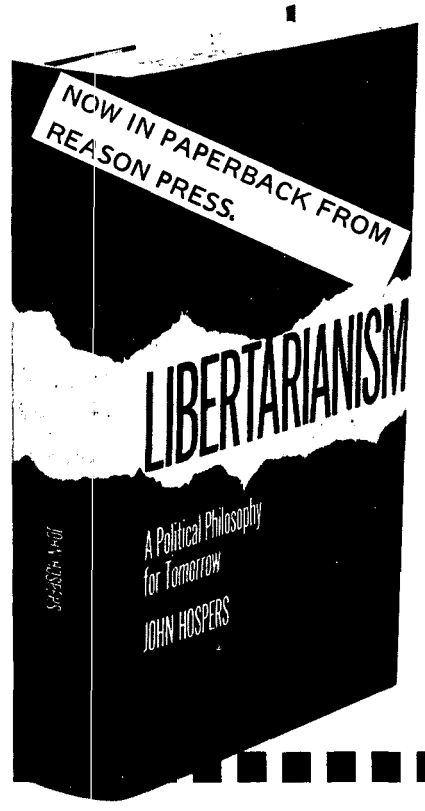

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Consider the power black-outs, fuel shortages, accelerated depreciation of the dollar, gold at the $150 per ounce level, and sky-rocketing food prices. Who expected this to happen with such magnitude so soon?

Consider also this: In view of deteriorating U. S. military, economic, and political conditions, it is likely that this country faces a catastrophic crisis in the near future. Nothing effective is being done to change the trend, and matters will get much worse before there is a reversal.

Therefore, as a measure of insurance, it is time to stock up on gold coins (if you have not already done so), plus a food supply which can be used in case of emergency, as well as for every day utilization, should nothing adverse occur. With passing time, acquisition of such a supply is becoming more costly.

Last year the U.S. had an overabundance of food. This year much of our food is in Russia, while some of our domestic prices (including prices of storable items such as wheat) are 3 times higher than previous to the give-away.

We have seen that farmers have killed newly hatched chickens, for the feed has become too expensive due to the "sale" to the Soviet Union. And the Secretary of Agriculture assured us that food rationing is unlikely. (Could anyone foresee the need for such "assurances" in 1972?)

During the last five years, we emphasized acquisition of gold coins as a security investment in our advertisements in the Wall Street Journal, Barron's, Human Events, American Opinion, Reason, and other publications. Those who bought these coins through us already realized great benefits. Now we are advocating acquisition of a ready reserve food supply also as a security investment. Reflection on the past and on what politicians have done and are doing to this country, show this to be necessary. (Thus, while in summer of 1973 it became known that our domestic granaries were almost depleted, a huge U. S. food sale to Red China, on extremely dubious terms, was announced. The food is to come from future crops, as there were practically no reserves left for use of the Red China transaction after shipment to the Soviet Union.)

Nearly all grocery stores now sell packaged and canned foods. However, these items are not designed for lengthy storage and quickly lose freshness and taste, as well as important vitamins. In addition, grocery store items take up considerable space and are heavy. Nor have the drying methods used for thousands of years for food storage proved satisfactory. Their appeal, even before becoming completely stale or spoiled, was always far from desirable. To correct this, the so-called "Low-Moisture" methods were developed about 23 years ago. Their value in providing fully adequate and attractive meals has since then been well proven. However, new developments in this field have improved these products even further. Low-moisture foods were used by the climbers of Mount Everest, and were taken along by our astronauts to the moon. Low-moisture foods are also completely practical and easy to prepare for normal, everyday household consumption. Yet, they last up to 15 years and longer without requiring refrigeration, while their reduction in weight and space of 75% (compared with grocery store items) makes it possible to keep a one or more year supply in a house or garage.

Our Salt Lake City processor has over 20 years of experience (it is the oldest in this field) in providing balanced, low-moisture foods which excel in nutrient, vitamin and mineral contents, as well as taste. The low-moisture methods used to achieve this require greater effort than the usual processes, but results—in terms of taste, nutrients, and longevity, as well as bulk and weight—are worth it. Moreover, cost to the consumer is surprisingly low. Fully adequate, appealing meals are provided at 48¢ each.

Expert design of the ready reserve food supply eliminates guess work as to what to store. This can be of utmost importance to health, especially if a food crisis persists longer than a few days. Fruits, vegetables, eggs, cheeses, grains, sugars, proteins, cooking aids, and a wide variety of other foods, certain to preclude monotony, are provided, together with a culinary book containing outstanding recipes, ideas, and suggestions for best utilization. You may use these foods in your everyday menu, while, at the same time, keeping enough in reserve against a food "black-out." (We can replenish your used up supplies as they are consumed.)

The desired results are achieved by: 1) dehydration of the food; 2) placing the dehydrated food in internally enamelled cans (of which 116 are the regular size #10 cans, each being slightly smaller than a gallon, while 8 are half-size #3 cans); 3) evacuating the air from the cans, replacing it with an oxygen free atmosphere and sealing the cans; 4) packing the cans in cartons of 7-3/8" by 12-3/4" by 18-3/4" dimensions. 20 such cartons weighing 600 pounds and occupying 2/3 of a cubic yard (you can fit them all in your car) provide a 12 month supply for 1 adult person at 2,450 calories per day. (The supply is so designed that either families or single or several adults may use it. While it may last 6 months for 2 adults, the proportional time decrease for a family with small children is less than for adults. Thus, for a family of 6 consisting of a father, mother, and 4 children aged 2 to 14 years, the supply will last longer than 2 months. This is because children consume less than adults.) Opening a sealed can will not cause spoilage for several months, thereby enabling full use of its ingredients.

The following is a list of the contents of the augmented yearly supply described here (except as indicated, all cans are #10 size):

FRUITS: After restitution with water, the same as 103 lbs. of fresh fruits, consisting of apples, peaches, and fruit galaxy of apricots, grapes and cherries, providing 521 of 3 ounce servings. 6 cans.

VEGETABLES: After restitution with water, the same as 268 lbs. of fresh vegetables, consisting of carrots, green beans, sweet corn, tomatoes, cabbage, potatoes and peas. This provides 500 of 4 ounce servings. 12 cans.

SUGAR: 36 lbs. of granulated sugar. This is more than sufficient for normal use of one year. 6 cans.

MILK: After adding water to the powdered milk, the yield is 230 quarts of non-fat milk. At normal consumption of ½ quart per day, this is sufficient for more than a year. 12 cans.

CONCENTRATED VEGETABLE PROTEINS: This category provides a meat substitute, equivalent to the protein content of 100 lbs. of lean, fresh

meat. Also 186 servings of bacon-flavored bits—excellent tasting. 12 cans.

GRAINS: Sufficient flour (or unground whole wheat, yielding the same amount) to provide 250 lbs. of rich, wholesome bread, or any other items the wheat may be used for. Also: 228 of 4 ounce servings of pinto beans; 84 of 4 ounce servings of quick cooking oats; 116 of 4 ounce servings of elbow macaroni; 96 of 4 ounce servings of yellow cornmeal; 279 of 4 ounce servings of rice. 42 cans.

EGGS: 384 eggs (32 dozen) in powdered form, providing more than one egg per day for a year. 4 cans.

CHEESE: 128 of one ounce servings of cheese. 1 can.

GELATIN DESSERT: 256 of 4 ounce servings of gelatin dessert. 2 cans.

BREAKFAST DRINK: 320 of 4 ounce servings of grape, grapefruit, orange, or pineapple drinks. 2 cans.

SHORTENING: 39 pounds. 12 cans.

MARGARINE: 10 pounds. 3 cans.

SUPPLEMENTS: Cornstarch sufficient to make 96 pounds of pies, or other uses; minced onions to provide 384 one ounce servings; beef bouillon for 218 servings of 6 fluid ounces each; chicken flavored and beef flavored gravy for 384 of 2 ounce servings; iodized salt sufficient for more than one year; adequate baking powder and yeast. 10 cans, of which 2 are #10 size (the same as all others listed above) while 8 are half-size #3 cans.

TOTAL: 116 #10 cans, 8 #3 cans; all packed in 20 cartons. (NOTE: none of the items listed here require special care or refrigeration for long term shelf life. However, yeast and baking powder will stay fresh longer if kept in cold storage.)

It can be seen that the READY RESERVE supply provides highly nutritious food, with a high protein, high mineral and vitamin content, sufficient for maintaining good health; and that the 2,450 calories per day, thus furnished for one year, are well balanced. While the food is easy to prepare and use, the book, CULINARY CAPERS, which comes with the supply, contains beneficial instructions and suggestions.

Cost of the yearly supply is **$528** plus shipping charges (varying between $30 and $80 depending on location). This is a bargain even if we never have a food "black-out." Thus, if nothing else, the ready reserve supply serves as a hedge against burgeoning prices. But, should a food crisis occur, the supply can be vital for sheer survival.

Also available: A 5 month READY RESERVE supply providing all necessary items for a 5 month period. This supply comes in 8 cases and weighs about 220 pounds. Cost is **$275** plus $20 to $50 shipping charges. The variety and quantity is smaller than for the yearly supply, but fully adequate nourishment is provided for a 5 month period.

A WATER PURIFIER, good for approximately 100 gallons, is included at no extra cost for the yearly as well as 5 month supplies. This is an exceptionally excellent item, removing contaminants (including radioactive particles) down to one micron (40 millionths of an inch) in size, thus providing pure, usable water, even from highly polluted sources.

Because of worsening inflation, we can expect further price increases. Therefore, we urge you not to delay even one day, as our politicians are not making things better for American consumers. If your order is received within 2 weeks after reading this notice, we will send free of charge as a bonus the two following important books: 1) PASSPORT TO SURVIVAL; 2) FAMOUS MORMON RECIPES.

All U. S. gold coins in uncirculated condition. All foreign gold coins in extra fine to uncirculated condition. Many other gold coins also available, plus uncirculated and circulated silver dollars and other silver coins.

IMPORTANT NOTICE:

Many persons wishing to have food insurance for themselves and/or families and short of cash, have asked us if the food can be obtained on a time payment basis. Nevada Coin Exchange is normally not receptive to sell on a basis which places customers more in debt. But, food is more vital for survival than any other purchasable item. Therefore, we made arrangements with Master Charge and BankAmericard to enable time payments (or cash pay-outs) with them for food. If you wish to use this service, please fill in your Master Charge or BankAmericard number as indicated on the order form.

FULL GUARANTEE:

If unsatisfied, you may return coins and/or food ordered to Nevada Coin Exchange within ten days for a complete refund of your purchase, plus a complete refund of any shipping charges.

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PLEASE SEND:

1. A _____ year(s) supply of READY RESERVE FOOD at **$528** per one year supply, or a 5 month supply of READY RESERVE FOOD for **$275** together with the book, CULINARY CAPERS and water purifier. If I ordered within 2 weeks from reading this notice, you are also to send me free of charge the books PASSPORT TO SURVIVAL, and FAMOUS MORMON RECIPES. I may obtain at request free information on hand or power grinders, water purifiers, breadmixers, survival and/or recipe books, and other supplies.

2. Gold coins (indicate type and quantity desired):
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   _____ pieces of Mexican 50 gold Pesos, containing 1.2056 Troy Ounce gold per coin.
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INVESTING IN RUBIES, SAPPHIRES, EMERALDS, & DIAMONDS

Bernard Zucker

The world-wide economic system is seriously out of balance. Even a casual reader of the newspaper can observe that almost all national economies are beset by shortages of goods, over-abundance of paper currency, and lack of inter-governmental cooperation. What can the average American citizen do to protect himself? In addition to careful investments of a conventional sort, I would suggest as a partial answer to these difficulties the purchase of a quantity of rubies, sapphires, emeralds, and diamonds for investment purposes.

Bernard Zucker received his A.B. in economics from Yale University and graduated from the Harvard Law School in 1965. He is an executive of the Precious Stones Company (rubies, sapphires and emeralds), in New York City. In addition to traveling throughout the world as a gem importer, he lectures on the history of illuminated manuscripts as well as Renaissance and post-Renaissance jewelry.

This past May, at a Sotheby Parke Bernet auction, a 44 carat sapphire sold for $200,000. Three years previously a stone of similar quality and size had been sold for $60,000. The Enid Haupt emerald, a 34.30 carat deep green stone, was sold at auction in New York City for $385,000—40 percent above what it had fetched four years before.

It is easier to study the results of the past 3000 years than it is to predict the next 6 months' price pattern in rubies, emeralds, sapphires, and diamonds. Investment prediction is essentially based on a study of the past. Santayana, the Spanish philosopher, wrote "History repeats itself —first as a tragedy, next as a comedy." Let us take a shortcut together through the history of gems and jewelry and try to understand what can be expected in 1974 from an investment in rubies, sapphires, emeralds and diamonds.

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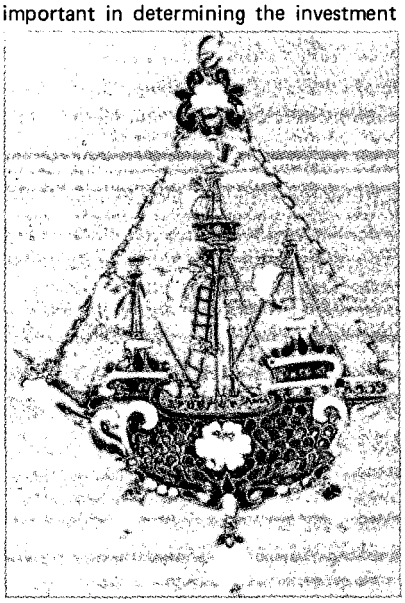
ANCIENT JEWELRY

In the Bible we find frequent references to rubies: "Who can find a virtuous woman? For her price is far above rubies." (Proverbs xxxi, 10) Where did these biblical rubies come from? Probably from the ruby mines at Mogok, Burma (where the finest shade of rubies are mined). Ruby mining has always been a primitive affair. The mine essentially is a well, hand-dug by a family of a few people, to a depth of perhaps 10 to 30 feet. A man is lowered by a rope pulley system to the bottom where he scrapes up layers of gravel. The gravel is then lifted by buckets to the top of the well. After the day's scraping is concluded, the man, his wife, children, and partners sort the gravel for possible ruby crystals. This system, though extremely primitive, is still used today because it prevents careless crushing of the fine and valuable crystals of ruby that are found haphazardly imbedded in the rock. At the Mogok mine site ancient cutting tools have been found, giving archeological proof that mining for ruby rough (as the uncut crystals are called) has been going on since prehistoric times. The chips of crystal rough are eventually cut and faceted and set in a piece of jewelry. The ruby may be shipped through a network of merchants to China, to the Middle East, and even as far as distant Europe.

Since Biblical times there has been a slow but constant evolution in emphasis, from the style and workmanship of the jewelry mounting to the stone itself. An analogy might be made: once the picture frame was important and ornate; now the canvas itself, often unframed, is the key value. This change in emphasis is very important in determining the investment value of a gem stone as well.



Venetian 16th century pendant, Morgan Collection, Metropolitan Museum of Art, New York.

Archeologists have discovered beautiful emerald necklaces from the early dynasties of Egypt. Although the settings are designed in a spectacularly simple manner, the emeralds themselves are generally of a poor quality and unfaceted. The gold workmanship, though, is of the highest standards.

Similarly, if we visit the Metropolitan Museum of Art in New York and see the fabulous Morgan Collection of Medieval and Renaissance jewelry, we can appreciate the extraordinary workmanship of European jewelry makers. The finest artists of the Renaissance had a much stricter period of apprenticeship than a painter today might have. Ghiberti, for example, began as a goldsmith in the 14th century and only later became a painter. Botticelli, a consummate painter, was also trained as a sculptor and goldsmith. The result of this interdisciplinary training was that jewelry was sculpted, crafted, and finished in an artistic and meticulous fashion.

In examining a boat-shaped pendant from the Venetian school of craftsmen of the 16th century in the Morgan Collection[1] we can see that the pendant, perhaps six inches high, is an exact scale reproduction of a Venetian trading ship. The sails are of finely worked gold, the bow of the ship is enameled, and natural pearls dangle playfully from the bow. Colored stones (rubies, sapphires, and emeralds) mined in India and in remote Burma stud the edges of the deck. These colored stones however were chosen primarily for their color. The style of the cutting was en cabochon—having a rounded top. If such a stone was faceted, the faceting was crude—en table—with only one rudimentary, flat surface.

Because the painters were also goldsmiths it is not surprising to find so many Medieval and Renaissance paintings accurately portraying the jewelry and gems worn by royalty and the wealthy. In the Vienna Art History Museum hangs Holbein's sumptuous portrait of Jane Seymour, Henry VIII's third wife.[2] She wears Burmese rubies and pearls in her hair in a piece of jewelry called a bordure. Around her neck is a jewelled collar called a carcanet, of sapphires, diamonds, and enamelled gold. Her dress is ridged with emeralds and pearls and the whole effect of blended jewelry and costume forms a breathtaking image of opulence.

THE FRENCH "SUN KING"

British opulence was far exceeded by the French Royalty. In the Court of Louis XIV, "The Sun King," gems and jewelry were an intrinsic part of the royal life style. Louis XIV used the vast amounts of gems he purchased to cement foreign

Holbein's portrait of Jane Seymour, third wife of Henry VIII, Vienna Art History Museum.

political marriages by giving enormous gem dowries to his relatives. He maintained the support of his noblemen by giving them extravagant gifts, and finally and most importantly, Louis used gems as collateral for the huge debts he owed the merchant bankers.

In the 1640's we hear of cutting stones in 16 facets.[3] What this means is that diamonds, now coming in increasing numbers from India and Brazil, could be cut and faceted to unlock the brilliance within the stone. Light could enter the stone and because of the phenomena of optical reflection and refraction could emerge and "sparkle."

The "Sun King" had many theories about how to live a civilized life. He had fairy tales read to him each night, never ate less than a 12 course meal served on golden plates, and felt that rubies, sapphires, and emeralds, because of their lovely colors, were appropriate for daytime wearing. Colorless diamonds would only be donned at night when their "fire" or brilliance could add magic to his candlelit dancing ballrooms.

An extraordinary thing happened to the "Sun King" late in his reign. A Scotsman named John Law (who had studied finance in Amsterdam and gambling in Venice) proposed to King Louis XIV that he issue paper money. I would suppose that after having spent his lifetime amongst the material, real world of brocades, rugs, tapestries, colored stones, diamonds, and silver and gold coins, Louis XIV thought this novel idea extremely bizarre. To ask a French subject to accept a piece of paper, in exchange for tangible gold or silver coin, seemed too ridiculous for words to Louis and he flatly refused.

After the death of Louis XIV, John

Law had greater success with the Duke of Orleans, Regent of France. The new government of France accepted John Law's proposal and the Scotsman became the most influential economist of his time. Money was printed and accepted and a great prosperity took place in France in the mid-18th century.

However, much like developments in our times, the French government secretly began to print vast amounts of paper money.[4] Gradually a discount was established between the worth of paper money and gold and silver coinage money. At this point John Law formulated his second great innovation—the flotation of a huge stock issue. With the Court's

Portrait of Henry VIII

approval he issued stock in a new company called "The Mississippi Company." This company had all rights to develop the vast territory called Louisiana in the western part of North America as well as parts of India and the Far East.

John Law had engravings printed showing the cliffs of Louisiana covered with emeralds![5] People were anxious to get rid of their devalued paper money and used it to buy shares of Mississippi Company stock. Prices boomed on the stock exchange. Mississippi Company stock offered at 400 French livres rose to 18,000 livres within three years' time. During this period of time the word millionaire first came into use.

The government printed and loaned more and more money to sustain and fuel this speculation. Prices for food, rent, and clothing increased astronomically, as could be expected. Paper money again started to sell at a discount to gold and silver coinage. Suddenly the stock market started to weaken and within a year completely collapsed. John Law fled to Venice and died penniless. Throughout this monumental collapse of the French economy, silver and gold coinage maintained its value, as did ruby, sapphire, emerald, and diamond jewelry.[6] This collapse so seriously weakened France that economic historians point to it as a causal factor of the French Revolution of 1789.

HOW TO DO IT

It is clear that throughout history gems have been a satisfactory alternative to paper money and common stock shares. For one who wishes to act on this knowledge, important practical questions remain: how and where do you buy a ruby, a sapphire, an emerald, or a diamond today? What do they cost? How do you judge the value of a gem stone? The answers are quite obvious. Just as people have come to rely less and less on their next door neighbor for medical advice and instead increasingly seek the help of a doctor or better still, a specialist, so, too, a specialist should be consulted when buying a gem for investment purposes. A reliable precious stones dealer or a fine jewelry firm with an outstanding reputation in the community is most likely to be the best guide to the investment possibilities in gems.

What is not often realized is that a dealer in gems sells a customer two things: the gem itself, and his advice concerning values and future values of the gem. That part of the price paid for advice is often a great bargain over a period of time.

The dealer should be able to educate the customer by showing him a large selection of rubies, sapphires, emeralds, and diamonds. The dealer should discuss the merits and demerits of each. Ultimately, however, the purchase of a gem stone will undoubtedly reflect the aesthetic choice of the buyer. Before arriving at the retail store, or at the dealer's office, I would recommend two preliminary steps: visits to the museum and a study of various gem books. These visits and books will reveal some of the following factors to be weighed in deciding how much and what to pay for a colored stone or diamond.

Rubies, sapphires, and emeralds appear in small amounts all over the world and are marketed in a completely competitive way in almost every major city in the world. Diamond sources, on the other hand, are highly industrialized and the supply is carefully managed by the marvelously efficient DeBeers Consolidated Mines, Ltd. (known in London as the Central Selling Organization). The difference between the marketing structure of these two—the colored stones and the diamonds—gives an investor two different investment possibilities.

THE COLORED STONE MARKET

The *ruby* is a red variety of aluminum oxide. The redness of this mineral species, corundum, is due to traces of chromium. While "A Rose is a Rose is a Rose," as we all know, red is not always red. Depending upon the shade of red, the size of the stone, and its freedom from internal flaws, you arrive at the proper valuation of a ruby. Judging the purity of the red, it must be remembered, is somewhat subjective and estimates will vary even between experienced reputable dealers. Assuming "near gem" color, a one carat ruby could sell for $10,000 per carat. The same "near gem" color in a ten carat stone could sell for $30,000 per carat or a total of $300,000 for the gem stone. Fine rubies above 5 carats are rare and above 10 carats almost unobtainable.

"Gem" ruby color is called by dealers pigeon-blood color. This trade term, used by experts who presumably have never seen pigeons' blood, is a velvety, deep red. The center of the red band on a color spectrum matches the red of a Burmese gem quality ruby. If you go to a florist and purchase a Happiness Rose, the intensity of the red in the rose should match the red of a Burmese faceted ruby. The ruby, therefore, combines the velvety feeling and the striking color shade of a rose. In addition, because of the faceting, it possesses the magical quality of "fire" or liveliness due to the light which is reflected and refracted within the stone.

If the ruby is not from Burma, its color will be a less pure deep red and may contain a darker red often with a touch of violet. These (mostly Thai) rubies will not contain tiny rutile needles (known as silk) which are minute crystals and indicate Burmese origin. Often what the Thai stone might lack in shade of color will be made up for in "fire" and in freedom from internal flaws. Thai ruby prices are significantly less than Burmese rubies but have been increasing rapidly.

In addition to Burma, Ceylon, and Thailand, rubies have been found in Africa, where the color is closer to a garnet-like darker, often violet red.

Burmese mine output has declined over the ages. There are extremely few new gem quality stones coming into the market. What is seen in the world gem markets and in the fine stores are old-mine Burmese rubies. These might be in the form of a round ruby bead, part of a Burmese necklace. Each bead can be cut into two pieces by a skilled cutter and faceted into a beautiful gem stone. A faceted Burmese stone which is in an old estate collection can also be removed from its mounting, recut, and made more beautiful.

Because of the rarity of the Burmese shade of color, more and more Thai rubies

are being accepted as close to gem quality. Besides the faceted ruby, rubies are also cut en cabochon. Some cabochons possess a star—or what gemologists call asterism—due to shafts of light which intersect within the ruby and channel light into whitish, relatively straight lines. The color of the finest gem star rubies is lighter and paler than pigeon blood faceted stones.

By leafing through gem books, one can get a clearer idea of the disposition of gem mines as well as pictures of gem quality stones. By going to museums you can see the actual stone and train your eye to get a feeling for the "platonic" perfect gem color. Seeing the shimmering red color of the Rosser Reeves star ruby in the Smithsonian Institute, or the delicate DeLong star ruby in the American Museum of Natural History is an important first step in gem appreciation.

Sapphire, like ruby, is also part of the corundum mineral group. Corundum which is not red is called sapphire. Sapphire's color comes from the traces of titanium, iron and chromium. The finest color in sapphire is deemed to be blue and the finest shade of blue comes close to the velvety blue of the cornflower, known as Kashmir color.

A one carat near-gem Kashmir color sapphire can be worth $3000 per carat and a near-gem two carat stone can reach a price of $4000 per carat. Sapphires of up to 50 carats are not unknown and larger sizes have reached prices above $5000 per carat.

In ancient times there were sapphire mines in Kashmir, India and that term is still used by dealers to denote this fine delicate color. Much more common than the Kashmir or Burma sapphire are the sapphires from Ceylon which are lighter in shade and often under a microscope or jeweler's loop evidence sharp liquid inclusions called feathers.

Fine quality sapphires are being mined in Thailand and just as Thai rubies are coming to occupy Burma's pride-of-place position, so too Thai sapphires are used as a substitute for the rare Kashmir sapphire.

Star Sapphires are more common than star rubies. The fine Star of India which is in the American Museum of Natural History can give one a fine idea of what a fabulous gem star can look like.

Green and yellow sapphires, fairly common, are much less desirable colors than blue sapphires although they have gained in popularity in the past few years. Prices are generally 80 percent less than the blue variety of sapphire.

Emerald green is not quite the color of "grass." Rather, its gem color is darker in hue. A fortunate visitor to the Shah's collection of emeralds and gems in Iran will immediately recognize the lively deep shade of fine Colombian emerald. Emerald is a beryl mineral species which contains traces of chromium to which it owes its color.

The finest examples come from Muzo or Chivor in Colombia. By the 18th century the Indian mines were played out. What remains today, aside from Colombian mines, are sites in Africa and Brazil.

The chromium in an emerald imposes pressure upon the atomic lattice structure of the emerald crystal so that it can rarely achieve a size over 12 inches. Large size emeralds, therefore, are a rarity. Emeralds are often criss-crossed with internal flaws —called by the trade "jardin"—or garden effects which seem to add to their organic appearance and do not overly detract from their value. A one carat near-gem color emerald can sell for upwards of $10,000 a carat and larger sizes can sell for even higher per carat.

The Haupt stone, auctioned at Parke-Bernet in New York, a 34.30 carat gem, has a tinge of yellow which heightens its organic feeling and also provides an indication of its Colombian origin. The $11,200 per carat price it fetched was not unexpected by the trade.

A dealer in colored stones, therefore, will be able to present to the investor a selection of rubies, sapphires, and emeralds and give him a choice of shade and nuance of color.

Today for the most part the value of the stone and not the setting will account for most of the value of the piece. In general it is more advisable to buy a smaller ruby, sapphire, and emerald that is free from internal flaws rather than a larger highly-flawed stone. There is a trade off between color and clarity. In other words a stone can have excellent clarity but poor color and often be worth as much as a stone with poor clarity and excellent color. In the long run, the more flawless stones have proven to be superior investments.

THE DIAMOND MARKET

The diamond is an entirely different form of investment proposition. In the late 1800's diamond mines of consequence were discovered in South Africa, larger than the previous Brazilian and Indian mines. Within two decades, with the help of Cecil Rhodes, a tight control over the South African production was achieved by the DeBeers Consolidated Mines Limited.

Unlike the family-type colored stone mining operation, DeBeers employs thousands of miners and centralizes the grading and processing of diamonds. Through extremely modern technological break-throughs DeBeers has managed to upgrade diamond production and standards through the years. The uncut rough crystals of diamonds are sent to London where a DeBeers wholly-owned subsidiary (the Central Selling Organization) 10 times a year ships a "sight" (a canvas sack of rough diamonds) to a select group of approximately 250 clients. As about 85 percent of the world's diamond output is purchased for resale by the Central Selling Organization, these "sights" greatly affect the world-wide diamond price. There is little room for bargaining and generally the distirbution clients accept their parcels of goods and either cut and polish the diamonds themselves or sell the canvas of rough diamonds to another dealer.

In an analysis of diamond price trends, economist Peter Crawford of First National City Bank said in the *NATIONAL JEWELER* (May 1973): "Assuming that diamond prices fluctuate with the overall price level, the level of stock prices and the price of gold, it turns out that the overall U.S. price level is by far the most important influence on diamond prices.

Portrait of Elizabeth I

"A statistical regression indicates that half carat diamond prices tend to rise by 13% or so for each 10% rise in the Consumer Price Index. Two carat diamond prices tend to rise about 20% for every 10% rise in the Consumer Price Index."

What this means is that over the last half century when the demand is there the Central Selling Organization has liquidated its diamond inventory at higher prices. When the demand has slackened the C.S.O. does not flood the market; on the contrary it releases fewer diamonds thus stabilizing the diamond price. The stated policy of DeBeers has been to maintain the diamond as a superior asset to paper currency. During the last two or three years the C.S.O. has been aware that the dollar and other currencies have lost a

great deal of their purchasing power. Accordingly it increased the price of rough to their dealers as well as markedly expanding the amount of rough sent from London. In 1973 the C.S.O. raised the price of diamonds on four different occasions and the total price increase averaged 70 percent. A very extraordinary year! DeBeers has also conducted a tasteful and effective advertising campaign throughout the world to win public confidence for the long term prospects and value of diamonds.

GRADING GEM STONES

When we speak of a one carat round perfect diamond we have a clear idea of what is meant. There are four factors in evaluating a gem stone: (1) its color; (2) the perfection of its cut; (3) freedom from internal flaws or fractures in the stone itself; (4) carat weight—the heavier the more valuable but a one carat highly spread diamond isn't worth as much as a perfectly proportioned 3/4 carat stone. The proportions affect the optical clarity of the diamond. The Gemological Institute of America with offices at 11940 San Vicente Blvd., Los Angeles, California, and 580 Fifth Ave., New York City, has perfected a uniquely accurate system of grading the color, the cutting perfection, and the clarity of diamonds. Therefore, if a diamond dealer in Buenos Aires telephones a dealer in Hong Kong and says he has a D-flawless, both parties understand each other. D refers to the color. Is it perfectly white? If so it is termed D color. Throughout the many diamond offices in the world a D colored sample stone is kept on record by the dealers. If a stone has a slight amount of yellow in it, it might be an E, F or G color. The term "flawless" means the stone is cut perfectly and is free from internal fractures. By having standardized the grading of diamonds the GIA completed the rationalization process for diamonds. In other words the diamond syndicate effectively controls the supply of rough (even though some believe the Soviet Union is starting to make inroads in DeBeers' hegemony) and the GIA has enabled diamond dealers to talk a common language.

A D-flawless one carat stone today could realize upwards of $5000 per carat. This price is well above the approximately $3000 per carat it fetched 18 months ago (although down from even higher levels several months ago). A two carat diamond normally sells at least 50 percent higher per carat than a one carat stone or approximately $8000 per carat. And price increases geometrically as the size increases. A price of $25,000 per carat for a very large size D-flawless diamond is not unreasonable. The all important certificate of D-flawless issued by the GIA gives the diamond the accolade of "gem." As the size goes down and the quality goes down the potential for value retention also declines.

Colored stones are in a completely different category. Although much research has been done on grading rubies, sapphires, and emeralds, if I telephone a dealer in Buenos Aires or in Tokyo I can tell him I have a beautiful red ruby but the exact shade of red cannot be transmitted over the telephone. Secondly, fractures are more diverse in colored stones and similarly cannot be graded by a uniform rating system. In addition, and most important for the investor, colored stones are not controlled by a central selling organization and are therefore sold strictly according to supply and demand.

OUTLOOK FOR THE INVESTOR

United States government import figures show the colored stone and diamond import values have increased sharply in the last 10 years. The value of imported ruby, sapphire, and emeralds has increased eightfold since 1964. The value of imported diamonds has increased fourfold since 1964. In 1964 $4 million of rubies and sapphires were imported and $3 million of emeralds were imported. In 1973 an estimated $24 million of rubies and sapphires and an estimated $36 million of emeralds entered the country. Total diamond imports (rough and cut) were $250 million in 1964 and an estimated $900 million in 1973.

What is the outlook for the coming year? The last 18 months have witnessed major rises of 100 percent on many qualities of gem rubies, sapphires, emeralds and diamonds. Japanese and European buyers moved both into and out of the market in large numbers. Barring a worldwide recession in 1974-75, I assume there would be a continued demand for precious stones. Softening in the Japanese market (which has occurred) might be met through increased demand from another increasingly prosperous section of the world.

The appreciation of a colored stone transcends language. A Chinese physician in Hong Kong, an Isphahani rug dealer, and a Rio de Janeiro auto executive will all be drawn to a fine colored stone. Unlike a Jackson Pollack modernistic painting or a Chinese Northern Sung scroll, one does not have to come from a certain cultural milieu to appreciate a fine shade of Burmese red.

Synthetic colored stones have not made inroads on the demand for ruby, sapphire and emeralds although they have been on the market for nearly 50 years. Genuine diamonds have been hurt by imitation only to a small degree. (Synthetic stones can be differentiated under the microscope from genuine stones through the presence of minute gas bubbles, straight striae or growth lines and through various spectroscopic difference.)

In addition to buying stones, you should also know the basics of selling them. Because of world-wide appreciation, a precious stone can and should be sold the same way it might be bought: through a specialist with a good reputation—a reputable dealer or a fine retail jewelry establishment. While it is true there is at least a 30 percent wholesale to retail mark-up on jewelry, the buyers' market is a competitive one. By using common sense and offering the stone to a highly reputable dealer, you can generally obtain a fair price.

Auction houses are another fine avenue of sale with world-wide selling facilities. It should be remembered that it takes time to dispose of a piece of jewelry through auction and, of course, there is a commission charge.

The Gemological Institute of America can study your diamond or colored stone. If it is a diamond, the Institute will provide you with an expert certification of its grade. If it is a colored stone, the Institute will not grade the stone but it will determine and issue a certificate stating whether it is genuine.

My recommendation is therefore not that you put *all* of your assets into rubies, sapphires, emeralds, and diamonds (which after all pay no dividends and are not quoted each day in the *WALL STREET JOURNAL*), but that you consider diversifying in part into them. Perhaps 20 percent of one's assets might be prudently placed into these gems. By so doing, one has an investment which can be readily sold at the present time and, if the last few thousand years of experience is an indication of the future, which represent a continuing source of value wherever men or women treasure beauty. ◻

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III

Wind. And we sleep on grass. Like hands.
Clasped together for shelter. And sun.
Steeping us in warmth and yellow.
Blown away. Returning. Gone.
We gather more into each other.
And listen:
Heartbeat. Wind in hair. His breathing.
Breathing moist and intimate. Along
the skin of shoulder. Neck.
While sun becomes perhaps.
And branches. Dignify with shadow.

Wendy McElroy

All night, the branches
wept under freezing rain.
Now, coldly coated,
their indifference is crystal—
skeletons of sun
and brittle air.

You poets call this lace?
It is the articulation
of trees
in winter.

Fred Hawley

IN AFTER DAYS

In after days when grasses high
O'er-top the stone where I shall lie,
Though ill or well the world adjust
My slender claim to honoured dust,
I shall not question nor reply.

I shall not see the morning sky;
I shall not hear the night-wind sigh;
I shall be mute, as all men must,
In after days.

But yet, now living, fain were I
That someone then should testify,
Saying—"He held his pen in trust
To Art, not serving shame or lust."
Will none?—Then let my memory die
In after days.

Austin Dobson

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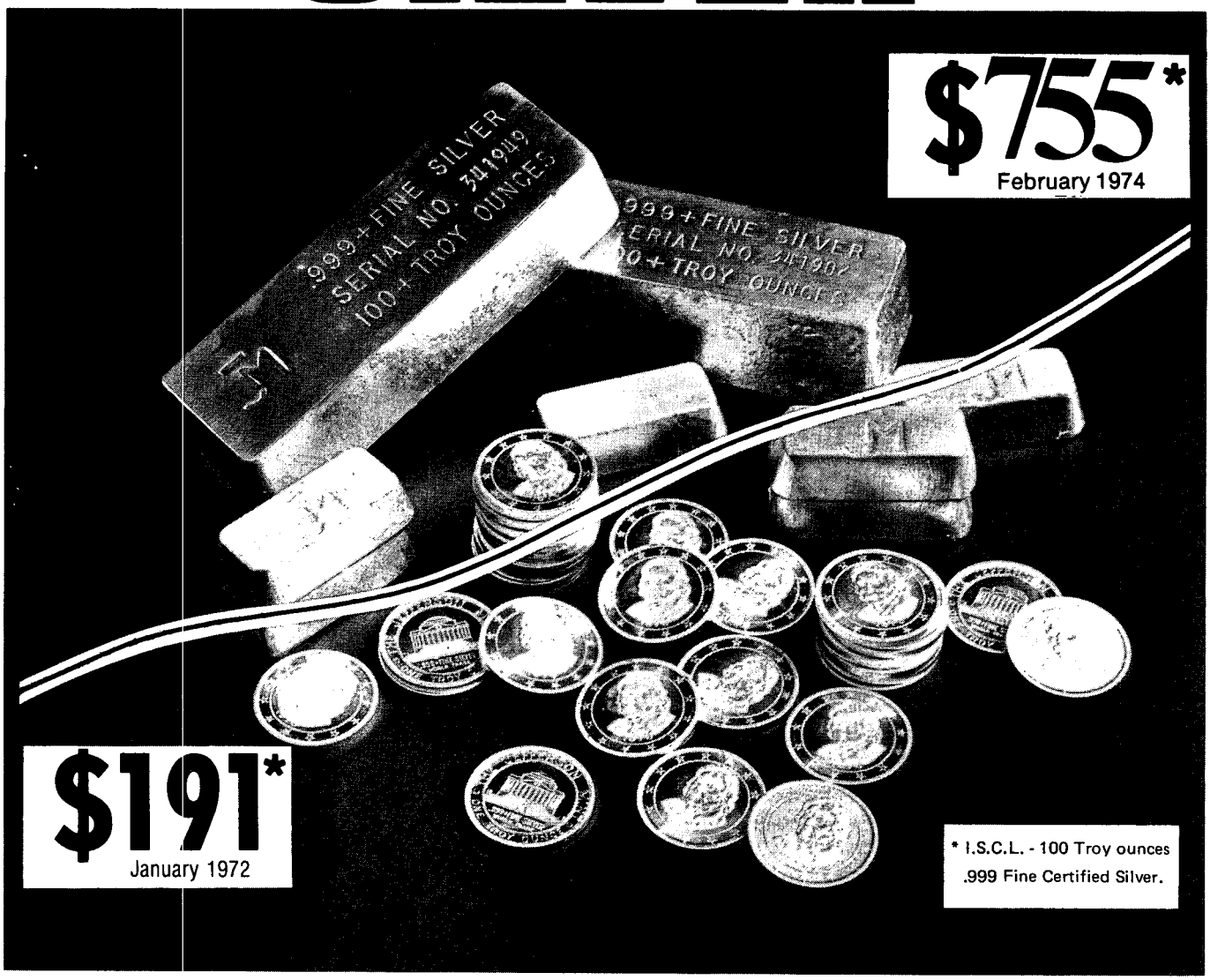

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If the Election on November 8 could be decided on the basis of truth and honesty, both sides would lose

Anyone who has read a newspaper in recent years knows what is happening in Washington.

It is bi-partisan corruption.

Things have gotten so bad it is no longer surprising to read that White House aides have been indicted for being "look-outs" in a burglary.

Or that the Attorney General of the United States was in direct control of a Mexican bank account used to finance illegal activities.

Or that a Congressman or Senator has been arrested for bribery.

And these are only the ones who are caught.

Since politicians have the power to make their crimes legal most of them are never brought to justice.

They peddle favors and influence to enrich special interests.

They vote themselves lavish raises and live in luxury while the taxpayers strain to make ends meet.

They buy votes by subsidizing inept companies and providing welfare to those who refuse to support themselves.

They have spawned a bureaucracy which meddles in everything. They even have inspectors going around the country measuring toilet bowls.

They treat us like morons instead of citizens. They boss us around, bus our children and raise our taxes to pay for it.

When they want our votes they will promise anything. But as soon as the election is over they forget their promises and ignore the opinions of the people.

Democrat or Republican, it makes no difference. All they are concerned about is their own power.

If America is to be saved, we must stop waiting for politicians to solve our problems. Politicians have solved nothing. They will solve nothing.

Only the people can save this great country. You, your neighbors, all of us who care must band together in a giant citizens' movement to rescue America from the politicans.

Together, we can force an end to the waste and corruption in Washington. With an independent and vigorous lobbying program, we can bring government under control before it swallows up everything. We can reduce taxes and inflation by demanding policies which benefit the people,not politicians.

If we join together, in a National Taxpayers Union, millions strong, we can make the politicans listen, no matter which of the losers win on November 8.

Let's make the politicans listen to us for a change.

National Taxpayers Union
325 Pennsylvania Ave. S.E.
Washington, D.C. 20003

I agree, it is time for a massive movement of concerned citizens to save America. Enclosed is my contribution to support this effort

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WHAT TO DO

I have met only two people in my whole adult life who professed a desire to pay taxes: a government professor and a lady canvassing for the League of Women Voters. Everyone else has had a sane dread of parting with large chunks of his money.

This may be why a Supreme Court Justice remarked that "taxes are the price we pay for civilization." Out in the backwoods, where primordial desires are given freer play, the revenooers have a distinctly hazardous job. Snuffy Smith doesn't pay anything on April 15th, and you wouldn't have to either if you wanted to slink off into the woods with your bear rifle.

The one big drawback of this sort of tax avoidance is that all the money you might save does you no good at all because you can't spend it. What you need is a way of avoiding taxes which still allows you to earn and spend as you see fit. The purpose of this article is to point the way toward such a possibility.

There are three means by which you might hope to be delivered of your tax burden. The first two, *legal tax avoidance* and *illegal tax evasion,* have the greatest immediate potential. The third, changing the entire system of confiscatory taxation, is mandatory for your long range economic security, but harder to effect. I shall treat the first two possibilities first and get them out of the way, before I lead you into the grim world of *tax rebellion.*

James Davidson is Executive Director of the National Taxpayers Union, a libertarian lobbying and political action organization. He was formerly publisher of INDIVIDUALIST.

AVOIDING TAXES . . . LEGALLY

A forthright discussion of tax avoidance is almost an impossibility, as it involves, inevitably, the complications of the tax code and innumerable IRS rulings. If there were any simple way to legally avoid taxes, Congress would come clamoring into special session and repeal it. The "tax loophole," so-called, originates as much from the fact that private lawyers and accountants are inevitably more clever than the Congressmen who write the laws as it does from the willingness of Congress to favor special interests. As long as the intelligence of the average Congressman remains what it is, tax avoidance is within the grasp of anyone who reads this journal.

One rule of thumb which is often overlooked by taxpayers is that contested tax assessments are generally settled more cheaply than when the taxpayer timidly agrees to IRS demands. In fact, the tax codes are so vague, and the factors in business and life so diverse, that no set tax can be said to be due. The appearance of uniformity in tax collection is only that—an appearance. It works to the benefit of the IRS in the case of the average taxpayer, whose income is garnished at the source by withholding. However, any person who has his money in hand on April 15th is in a good bargaining position. When former Solicitor General Erwin Griswold was Dean of Harvard Law School, he remarked that ordinary wage earners may be the only taxpayers who ever pay the set rates for their income brackets. More flexible rates are in effect for you if you have the ingenuity to use

ABOUT TAXES

James Dale Davidson

them.

When *WALL STREET JOURNAL* reporters took identical information to five different IRS offices, the computation of tax owed came back five different ways. This underlines the basic importance of making your business affairs seem complicated. If they are, and you have enough bluster and an accountant, you can get away with paying far less. It is much like poker. If the IRS can make you fold early, you pay a higher rate. If you hold out through the first appeal process, you can settle for an average of 42¢ on the dollar of tax allegedly due. If you can raise the ante still further, and go on to the IRS appellate division, you can settle for an average of only 35¢. As in poker, it pays to have nerves of steel.

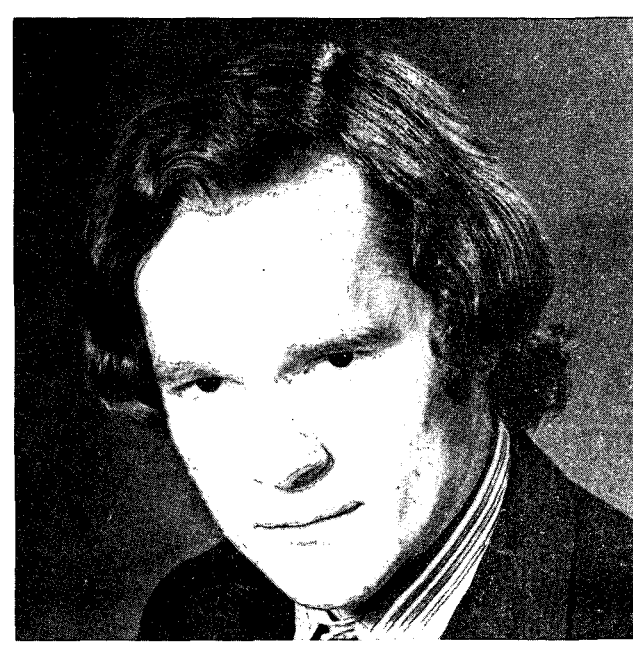
The peculiarities of your own circumstance will determine what tax dodge is best suited to your needs. Just remember that, except for the poor sap at the bottom, there is no such thing as "*the* tax rate." There are many tax rates. It is your task to pick the lowest possible one.

EVADING TAXES

But what about tax evasion? This is a subject which interests many people but which is almost never written about. This is not because it is particularly obscure. Rather, almost everyone who knows about it has more at stake in keeping quiet than in spelling it all out. Not a little consideration is the fear that the IRS will pounce upon the blabbermouth who writes about evasion, thus making him pay dearly for divulging the tricks of the trade. I am not susceptible to this inhibition only because I *already* expect the IRS to go over my return with a fine-toothed comb.

So what do you do to evade taxes? What you *don't* do is claim a lot of phony exemptions, although that might work if you have a limited income. Also, don't give your dog a Christian name and enroll it in the university. They'll eventually catch on. You have to play it straight when it comes to number of dependents and other obvious frauds.

If you want to get into tax evasion, do it as the experts do. There are a million ways in this world



MILWAUKEE JOURNAL PHOTO

to make money which cannot be traced. Many of them involve hocus-pocus with foreign bank accounts and transfer of funds internationally. Because most foreign countries don't consider tax evasion a crime there are refuges abroad where you can do business under the name of some company off the *MONOPOLY* board.

The secret, foreign bank account, therefore, is essential to your evasion scheme. Once income is hidden from the government in some safe repository, such as a Swiss bank, innumerable opportunities arise. For example, after an anonymous deposit is made, the depositor can secure a "loan" (really only a withdrawal) from the bank and then deduct the "interest" payable from his gross earnings at tax time.

Another common and profitable means of earning tax free money is trading securities through a Swiss bank. Since Swiss banks are registered security brokers, a person possessing an account can anonymously trade in securities in the bank's name and then hide any resulting gains from the IRS. When you deal through a Swiss bank, you need pay only Swiss taxes on dividends, while the major profit area, capital gains, remains untaxed. Since Swiss banks account for 20 percent of all trading on the New York Stock Exchange, you may have fallen behind the Joneses if your stock dealings are not already sheltered in Switzerland.

"Contested tax assessments are generally settled more cheaply than when the taxpayer timidly agrees to IRS demands."

But, if you don't like the Swiss for some reason, don't let that stop you. There are other nations where bank secrecy laws are in effect: the Bahamas, Curacao, Mexico, Panama and Liechtenstein. You can have your funds transferred to one of these exotic and profitable spots through a variety of ruses. One common practice is to write a contract with a foreign exporter to purchase "widgets" at far above the normal price. The invoice is marked up from, say $100 to $200 each. The additional $100 is then deposited by the exporter in your name in a foreign bank (less, of course, his fee for playing along, which he will probably deposit in his *own* Swiss bank account). Then you can turn around and sell your widgets in the United States. If you can only unload them for $170 each, you have an additional $30 loss for each widget to write-off at tax time. Or you may want to follow an increasingly popular practice of starting your own foreign corporation to serve the function of foreign exporter, thereby eliminating the need for the middleman.

"Once income is hidden from the government in some safe repository, such as a Swiss bank, innumerable opportunities arise."

There are many imaginative ways of repatriating the money if and when the time comes. One method is to have the bank, acting as a trust, purchase some valuable asset from you. You get your money back and you still own the property through your trust in Switzerland.

AN INTERNATIONAL PASTIME

These are just a few of the many ways to evade taxes. If you think about it for a while, new and more daring methods will occur to you, of the sort which have been fascinating individuals in most other countries of the world. The belief that tax evasion is wrong is a peculiarly American hang-up. There is no inherent reason why you, as an American, should be any less effective at evading taxes than, for example, an Italian. A parliamentary study there showed that Italians will gladly use any and all gimmicks to evade payment. For about eight million individuals and firms, this includes failing to file any return whatever!

Of course, you probably can't match up to the Italians by suddenly failing to file a return. But you can work up to it through the ultimate evasion—"premature death." You arrange your affairs so that you receive income in cash, perhaps even by shifting businesses temporarily. Then, you pretend to die. You have an estate tax filed, and automatically the IRS halts any investigation it may have had underway for deficiencies in previous years. If you've prepared things properly, all your property and wealth has already been transferred to you through your Swiss bank. When the IRS comes for as much of your estate as can be carried away, they come up empty-handed. And they're not even surprised because so many poor saps in this country die penniless that you're just one in the crowd.

The unfortunate thing about feigned death as a tax dodge is that it almost makes sense. And that is sad. It shows how far we have departed from the concept of a free society as it was known and realized by our forefathers. Now only the most clever, resourceful persons can make it and keep it in an environment choked by government. The vast majority has helplessly watched its living standards decline over the past few years. And with taxes likely to go even higher, this decline will become more sharply evident. Not surprisingly, therefore, people are deeply

troubled. Their homes, in many instances, are being taxed away. Their savings and hard work are eroded by inflation. Their small businesses are folding under pressure of taxes and bureaucracy.

CHANGING THE SYSTEM

This brings us to the point where ideology must enter your tax avoidance plans. Let's face it, you're never going to get away with surviving and prospering in a society where everyone else is smarting under the sense of deep personal loss. Envy is always accentuated in times of trouble, as it affords the majority a means, no matter how irrational, of easing its distress over exceptional success while everyone else is failing. The fervor with which popular opinion has turned against so-called "tax loopholes" provides an instructive lesson. Unless there is a revolution in the attitudes of the American people you might as well go out and join Snuffy Smith right now. Because you'll almost have to live isolated in the woods to avoid what's likely to happen when our overtaxed economy finally breaks down. Under such circumstances, which are described quite plausibly in the new book by Roberto Vacca, *THE COMING DARK AGE,* markets would be interrupted, power and transportation systems would collapse, rioting and violence would be endemic. The only way this can be avoided is through an ideological re-orientation of the American people.

I am not going to tell you it's your duty to take part in this effort. However it is certainly to your benefit. No matter what you have thought or done about political or ideological questions in the past, your own life is a revealed demonstration of your values. If you picked up this magazine to find out how to make money for yourself, whether in bonds, precious metals, or the arbitrage of pork bellies, then you are the sort of person who has a stake in preserving free enterprise.

This means that you would probably find it profitable for the future to contribute a share of your present income, say part of that which you save by more active tax avoidance, to support agitation for a free market. This is a cheap and effective way of forestalling the possibility that you'll have to run off to your country place to live off the land a few years from now. In that case, all the money in your Swiss bank wouldn't do you much good. Unless you have an ocean-going sail boat, you might not be able to get at it.

It has become a cliche among many people that no amount of free enterprise agitation has any effect in retarding the growth of big government. This is false. Actions which failed in the past often were unsuccessful because there was no suitable organizational vehicle. Groups such as the Chamber of Commerce probably set the cause back because their arguments for free enterprise have been too half-hearted. Members of the public have discerned no great principles at work and no benefit to themselves

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from the sporadic business-oriented campaigns for lower taxes.

But in some circumstances, however, people are willing to listen. A highly principled campaign, appealing directly to the intelligent person's self-interest, may succeed where lesser efforts fail. The task in America is to achieve a progressive movement committed to tax reduction and the free market.

That this is both possible and popular may be gleaned from the success of Mogens Glistrup in Denmark. In only one year since its founding, Glistrup's Progress party has grown to be the second largest in the Danish parliament. The Glistrup platform, popularized at campaign rallies where voters paid $2.50 to hear him speak, includes complete abolition of income tax over a five-year period, firing of 90 percent of all Danish government employees, elimination of government rent controls, abolition of the Danish military, and re-writing of all laws so they are short and clear enough that everyone can understand what they mean.

"The belief that tax evasion is wrong is a peculiarly American hang-up."

That Glistrup's message is being heard can be gathered not only from his spectacular electoral success, but from the fact that he has been bitterly attacked by advocates of big government in other countries. Two days after the Danish elections last fall, no less than the *NEW YORK TIMES* ran a bitter editorial denouncing Glistrup's "quack doctrines" and his appeal to a "mindless following." It is clear from the *TIMES'* reaction that the good government crowd in charge of its editorial room sees the relevance of tax rebellion to America. If the citizens of the pluperfect Scandinavian welfare states are fed up, Americans might come to be equally upset if they could be induced to sit down with their scratch pads and figure out just what big government does—or doesn't do—for them. Let that day come, as the *NEW YORK TIMES* fears, and the antitax message of the sort which Glistrup peddles could sell, even in the outlying boroughs of New York City.

A NEW AMERICAN REVOLUTION

Another amazing thing about Glistrup's success is the fact that he is generally considered a progressive in Denmark. To his fellow Danes, he is a man with new ideas and new ways of thinking which challenge old policies. Libertarians here in America can earn that same respect with clear calls for radical tax reduction and elimination of bureaucracy. There is no longer a paucity of evidence about the effects of giant government spending programs. Every day brings some new proof: another study; some more facts and figures buttressing the free market view. This information must be transformed, through agitation and advertisement into a new American Revolution, of the sort which gave our forefathers their start two hundred years ago. John Adams wrote that this Revolution was not a war. Rather, "The Revolution was in the minds and hearts of the people; a change in their religious sentiments, of their duties and obligations .... This radical change in the principles, opinions, sentiments, and affections of the people was the real American Revolution." So said John Adams, who should have known. And so it could be today.

Through support of agitation, tax resistance, local organizing, and court action you can achieve something more important for your future than any technical adjustment of the tax codes, or repeal of the interest equalization tax. You can gain a civilized climate in which to live and trade, one where you can prosper without hindrance or favor.

But if you let the chance to achieve a free market society in America pass without doing anything about it, you'll suffer even if you are clever enough to have stashed away all you need to survive on some mountain top. This is because you'll end up with less than you would have had to settle for otherwise. When society suffers from overtaxation and bureaucratic control, you lose services, inventions, art, literature, entertainment and companionship that might otherwise have been at your disposal. Civilization, as Murray Rothbard has aptly noted, is a "free ride." When everyone is wrapped up in an autistic struggle to survive, the "free ride" won't take you half as far as it should. "The Coming Dark Age" which Vacca describes could really be just *that,* with insufficient capital to sustain enterprise and little leisure to allow contemplation of any sort. Philosophy and art under such conditions would be impossible. That much Aristotle makes clear in the first chapter of *METAPHYSICS.*

Rather than allowing life to sink back into the philosophic and moral abyss from which Man has struggled so long to emerge, you can enhance your own life by working to prevent it. Not only will you likely reap material rewards, but you will also set yourself in line for undoubted benefits of a less tangible nature. If you ever had even an inkling of a desire to achieve something noble or useful in your life, working to help achieve a free market could be just that. As John Milton wrote, "What can be nobler or more useful in human affairs that the vindication of Liberty?"

With this in mind you can save yourself money and still help make a new version of the old dictum about taxes and civilization. You can avoid taxes. And you can evade taxes. But opposing taxes is the price you pay for civilization. ◻

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What, Exactly, is Going On?

—In *stocks* and *bonds*: the market is as treacherous as a mine field.
—In *real estate*: prices are at an all time high—but virtually nobody can buy or sell because there's no mortgage money around.
—*Shortages*: they're showing up everywhere! Paper goods. Lumber. Fuel oil and gas. Electricity. Steel. Food. *What next?*
—*Cash* and *savings*: you earn 8% to 8-1/2% interest—and lose 15% to inflation!
—*Precious metals*: values bounce around like ping-pong balls in unpredictable fashion.

What is going on? Let me tell you: we are witnessing new economic patterns unlike anything we have seen in this lifetime. We are witnessing inflation with rising prices and critical shortages—some very real—some imaginary, but carefully staged for the benefit of a few shrewd companies or individuals. We are observing a world that, despite short term fluctuations, is openly expressing its mistrust of the value of our dollars. And we are witnessing the world's superpowers teetering precariously on the brink of runaway inflation, depression, or *both*.

The next few years will belong to those who understand that *these new economic patterns are still based on the natural economic laws that are as old as civilization*: supply and demand, self-interest and greed; the domination of the blind and the faint-hearted by those who have the courage to *act* rather than to foolishly do *nothing* while "hoping for things to get better."

There is a selct group of men in this country who long ago predicted the approaching crisis . . . and who now can see clearly into the future because they have never been blinded by fairy-tale economics. They have been in close touch with each other, while the rest of the world has chosen pretty much to ignore them . . . and *many of them have already made great fortunes* by acting upon their own predictions about gold, silver, coins, mining stocks, etc.

The publisher of *Human Events*, the Washington newsweekly, has invited the most brilliant of these economic clearthinkers to join in the publication of a new bi-weekly letter.

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. . . which is intended to show you, *in simple, non-technical English, how to capitalize on the financial blindness of others*, and avoid the consequences of our nation's tremendous economic mistakes. The *Inflation Survival Letter* will also keep you informed of latest worldwide economic and political realities that bear on the inflation-depression crisis. Since most of the mass media will continue to ignore these realities, chances are that most of this critical news and economic analysis will be found only in the *Inflation Survival Letter*. *ISL* will cover coins and precious metals, gold shares, commodities, agriculture, legislation and legal decisions, the energy supply, international trade, science—*every* topic that effects your assets—and their future value. Typical of the subjects that are covered:

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- How to "read between the lines" of your newspaper to spot upcoming price rises or major economic upheavals.
- How inflation and depression will affect you if you are involved in a pension plan, deferred tax plan or trust fund.
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- Common sense guidance on choosing, buying and supplying that rural "hideaway" if the worst happens, and complete nationwide economic collapse brings on civil riots.

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Oakley R. Bramble, one of the very first economic analysts to publicly recognize gold and silver coins as an inflation-proof investment, is the editor of the *Inflation Survival Letter*. Formerly editor of the economic letter *Agora*, Bramble's keen economic insights combined with a lifelong career as a writer and journalist have for forty years helped thousands of men and women survive and even profit from inflation.

Among the other regular contributors:

- *John McFalls* is proprietor of Value Action advisory service, Seattle, Washington. The value of his model gold investment portfolio has tripled in the past six years.
- *Dr. Hans F. Sennholz*, head of the Department of Economics of Grove City College, Grove City, Pa., is one of the world's leading monetary economists.
- *Douglas Johnston*, vice president of the stock brokerage firm of First of Texas, is well and favorably known for his accurate predictions of the gold price break-out in 1973.
- *Henry Hazlitt* is one of America's best known economists. His book "Economics in One Lesson" is the most widely read non-technical book on the subject.
- *Dr. Murray Rothbard* is the leading libertarian theorist in the United States. His first book, "America's Great Depression" (1963) has become an incredibly accurate blueprint of the economic woes which have beset the nation in the past 10 years.
- *Alden Rice Wells* of Exeter, N.H., is both a stock broker and an investment advisor of worldwide renown. His "Monthly Report" and "Quarterly Report" are bibles for "hard-money" investors.
- *Congressman Philip M. Crane* is the leading Congressional force behind legislation to return the legal rights of gold ownership to the American people.
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- *Donald I. Rogers'* books include "The Day the Market Crashed" and many others. Formerly the financial editor of the New York *Herald Tribune*, Rogers is now president of American Economic Foundation.
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If, after receiving 3 or 4 issues, I do not see how the *Inflation Survival Letter* can help make my worldly goods inflation-proof and depression-proof, you will immediately *cancel* my subscription and *refund my entire $15 payment* at once—no questions asked. I may keep my free gift copy of the *Inflation Survival Manual* without cost.

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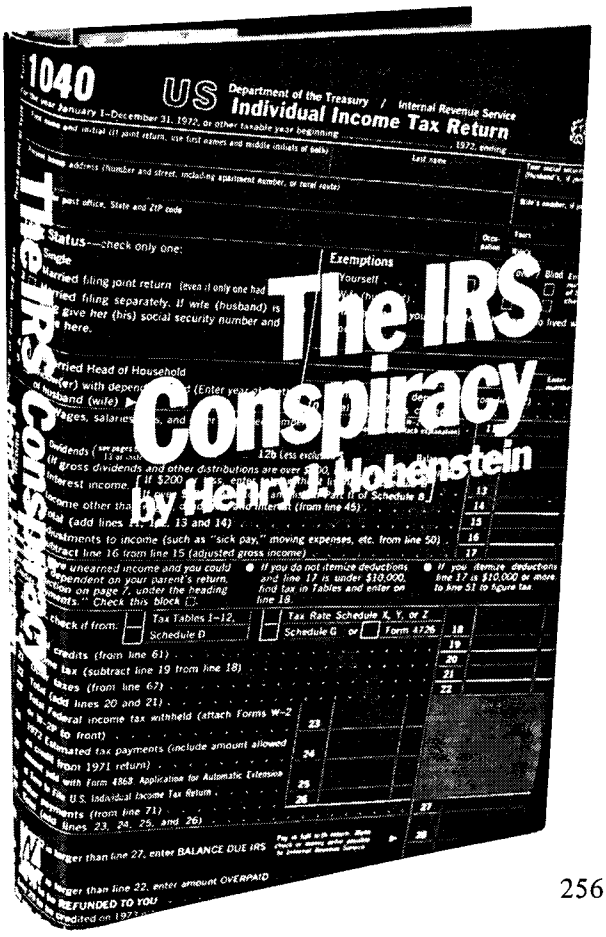
The IRS Conspiracy by Henry Hohenstein



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This book is a real eye-opener! The author shows, through documented facts and case histories, that our form of taxation is not only essentially immoral, but also that those programs subsidized and supported through taxes do not effectively work. We have all become victims of the IRS conspiracy, says Henry Hohenstein, and he tells what we can and should be doing about it.

Taxes are essentially ineffective, says Mr. Hohenstein, because, being progressive, they reduce the incentive to earn money and the individual feels his income is being drained away. Therefore, many people try, at their peril; to avoid payment of taxes and are charged with various crimes by the Internal Revenue Service. He cites case histories involving attempted tax-avoidance and the subsequent, astonishing methods used by the IRS to obtain payment. And because the service operates outside the judicial system and is not answerable to any other branch of government, the individual has no recourse in appealing to higher authority!

What's more, the IRS is committing a gross invasion of privacy. The government is made privy to certain kinds of personal information that is not normally even given to one's intimate friends, and the IRS can investigate areas of a person's life using methods that would be considered totally illegal if utilized by any other organization.

Mr. Hohenstein goes on to cite cases of individuals and institutions (many of them are nationally renowned) who advocate government subsidy of various programs, and who do not themselves pay taxes–therefore forcing others to finance projects in which they have no interest. Many of these projects (including such things as war, welfare, etc.) would either be nonexistant or else operate far more effectively in a free market context, says the author.

Mr. Hohenstein does not advocate an abrupt stop to taxation, for that would mean the collapse of our society as it is presently set up. But he does offer workable solutions to the current tax mess–it can be made more equitable only if the public is *informed,* and that is the purpose of this important book.

HENRY HOHENSTEIN is a writer, lecturer, and financial consultant. He was graduated from Rutgers University where he was a Delta Phi Scholar. Mr. Hohenstein has appeared on numerous national television and radio talk shows and has both interviewed national personalities and been interviewed by major newspapers and magazines, most recently by the *Washington Post* and *Time.* He was born in New York and currently lives with his wife and five children in Rolling Hills, California.

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If You Had Lived At The Time Of The Boston Tea Party And The Sons Of Liberty Had Come To Your Door –

Would You Have Joined Them?

The two hundredth anniversary of the Boston Tea Party passed last year with almost no notice. This bold tax protest by your ancestors is recognized by historians as playing a leading role in the shaping of America. Yet, as we look back today, the taxes which those early Americans fought seem trivial. Your own tax burden is now more than 1000 times greater than the taxes exacted by King George.

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The Time Machine

Harry D. Schultz

The year is *1985* and I stand here looking back over a decade of monetary and political history. It's funny. While we were living through the messes they somehow didn't seem nearly as bad as they now look in retrospect.

Gold never *was* revalued in terms of the dollar. Oh yes--it was revalued in terms of SDR's, which meant nobody really knew what that meant. The price of free gold relative to the dollar, the Swiss franc, the French franc, the pound, the deutsche mark (DM) and indeed every currency of every country where gold is *traded* now quotes the price of gold in its *own* currency. It happened slowly over the years. More and more exchanges stopped quoting the price of gold in anything but their own currency. So now we're back to more or less fixed exchange rates and a gold exchange standard, based on gold and the new SDR's and all currencies. Gold in terms of SDR's is now four times as high in price as it was 10 years ago, but then SDR's always were a bit arbitrary, like the DM after World War II. It took them till 1978 to really find their own level. SDR's have been changed to "IMU's" but they still aren't used much.

Gold in terms of the dollar is now *officially* $200. Americans can legally buy gold now but exchange control is so tight they can't buy *much* since that would involve sending money abroad. The value of the dollar on any international market is completely arbitrary; like the official exchange price of the ruble, the dollar/gold exchange rate only applies at home.

SOUND AS A DOLLAR?

Funny. In 1973 I predicted that the dollar would suffer many devaluations and become like a cruzeiro. It didn't happen. It was devalued by about 20 percent in 1974 as part of the monetary reform kick, when the world officially went off the dollar standard but didn't tell anybody it was doing so. But since then there has been no devaluation. Not for *us* these Latin four to five devaluations a year, said the U.S. Treasury. We are *above* that. *Instead* the Europeans have *revalued* constantly among themselves. No, it has never been *official*. Now when one goes to Switzerland *from* the U.S., the banks in New York give us one for one, i.e., one Swiss franc for one dollar, and we get 75 pfennigs for the dollar in N.Y., when we want to go to Germany. But it's different coming the other way. Nowhere in Europe will they give you more than *half* a Swiss franc or 40 pfennigs for your dollar. So the official rate is something that applies to Americans inside the U.S., on their travel allowance. This means the *true* dollar price of gold is about $400.

"Of course the bright Americans got their money out of the country before the controls began."

Really they don't need exchange control. Few Americans travel anymore anyway, except the handful who make killings on the fluctuating exchange rates. Yes, in this way we are very like South America; the rich get richer and the poor we try to hide away. When bread cost $5 a loaf what can you do?

But Europe has had her problems too and, indeed, Germany has become more like Finland than truly part of either East or West. Switzerland has lost much of her international banking status, partly because of the increasing inefficiency of her bank

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The text of this article is an address by Dr. Schultz to the International Monetary Seminar in Montreal last November.

staff which frustrated foreigners too much, and partly because with increasing exchange controls around the world fewer and fewer people were ABLE to invest their money through Switzerland.

The Arabs still do well there, and Switzerland still is as international as anywhere, and efficient enough for its vastly diminished business—especially as everywhere else is a whole lot worse. Germany fights an increasing trend towards socialism, a brand of socialism peculiarly German, certainly nothing like Russian socialism, in fact perhaps more like Swedish socialism with an edge of violence. However the trend has isolated her. Then there were Germany's futile attempts to be nice to the East in hopes that one day the country might be united. To the *Russians* friendship has always meant weakness and they took advantage of it; so Germany now sits in a no-man's-land twixt East and West. And even though people still buy German products abroad, her currency, while technically strong, is suspect by foreigners, and much of her trading is done in Swiss francs or in the new European unit of exchange. Oh yes—that was a strange story too.

After much economic fighting, the Europeans and the Americans went their various ways monetarily, and the entire EEC produced this European franc (as it was nicknamed)—a currency unit in which gold and all European currencies were defined. The idea was that their currencies and gold would move as a unit. The first country to fall out of the system was Britain, to no one's surprise. The British pound these days trades at £2 to one dollar. Then the Common Market itself fell apart, with France creating the first real break when she had an abortive *coup d'etat* in 1977. It failed, but the shock of a possible military state in France badly weakened the French franc for the rest of the decade; and Belgium suffered because of France, her currency being closely tied.

The Scandanavians continued their spiral of relative prosperity and inflation hand in hand (I have never understood how they do that). So the *European* franc is now a Unit of Exchange basically for the *Germanic* countries—Switzerland, Austria and Germany, with the rest of Europe redefining their own currencies in terms of it from time to time.

DEATH OF THE DOW

I regret the passing of the Dow Jones Average. With so much fluctuating of currencies, and with more and more socialism at home, the stock market ceased to be the main arm of capitalism and became the tool of the few opportunists with money, to preserve a constant value in an age of inflation. The names or balance sheets of the companies didn't really matter anymore. They were doctored anyway. Yes the SEC and IRS try to keep up with offenders, but no policing or revenue service can operate efficiently when inflation continues so fast as to outpace the value of taxes as well as income. So in 1979 it seemed only logical to create just one index of 1000 stocks. Now we have the "Wall Street Stock Average." It has been dull in the last five years, moving completely sideways.

"Nobody comes for you in the night, but you can die of sheer harassment from the IRS."

Americans who have a speculator's bent put their money in offshore companies, traded land, financed ships, or even traded the constantly changing exchange rates around the world. Sure these things are illegal with exchange control, but Americans are historically good at "angles" and loopholes—still do it with complicated tax structures and excuses to start businesses abroad when special permission is then granted to take money out. And of course the bright ones got their money out of the country before the controls began. It is impossible to make anybody say what he has abroad. With so *many* controls the sheer mechanics of government, like South America, has become too cumbersome to properly enforce. Thank God it is also very inefficient.

Oh yes, business *functions,* but nobody talks about growth rates anymore. People tend to make financial killings or go broke; they don't often grow healthily and slowly in business ventures.

SUBTLE TYRANNY

Funny how I also thought America could very easily become a police state with a dictator when I looked forward in 1973. That didn't happen either.

Well, not exactly. It takes a certain energy of idealism to create dictatorship, and somehow the death of the American way of life was so slow and penetrating that few people had any idealism *left* that could be stirred into revolutionary fervour. Sure, people *tried* but they failed. The U.S. is a police state in 1985 and yet it is not. Americans are free to travel and yet have no way of legally getting enough money *out* to travel freely. Politicians didn't erect an Iron Curtain; they merely made it impossible to arrange the air or boat fare to leave, or stay abroad. Nobody comes for you in the night, but you can die of sheer harassment from the IRS, especially if you say something against the President. They never enforced curfews but go out after dark and your life is as much in danger as it would be if the Army were on the streets with machine guns and orders to shoot on sight.

England has had *her* problems too. The IRA finally got the British Army out of Northern Ireland. But only because they created virtual civil war in England, requiring the Army on the streets of London and Manchester!

In these last 12 years much has happened in other parts of the world. Japan took over the entire Pacific basin. Her 1940 dream of a coprosperity sphere is now a reality. The yen is now 50 percent backed by gold. She has become the strongest trading nation in the world and is the *major* voice at all monetary meetings.

Latin America is finally emerging out of underdeveloped status, thanks to the proper use of raw materials. Currencies are improved in most cases.

Canada has become much more independent of the U.S.A., through diversifying her trading patterns. A political leader was elected in the late 1970's on a platform of breaking the umbilical cord with the U.S. It has been healthy, for no country should be so dependent on any other nation for so much of its trade. It has made for a friendlier feeling on both sides of the border.

Australia somehow survived its Labor government, which set it back dramatically. The new Conservative government has reversed all the old policies and the land down-under is booming again. Over one million Americans live there now.

Africa was the most war torn continent in the world in the past 12 years. Civil wars and small border wars have been unending. South Africa has modified her separate development rules, softened the rigid class barriers and has established good relations with several of her all-black neighbors.

China has emerged increasingly as a trading nation and her voice is heard more politically. But it will be several more decades before she is fully integrated into the outside world.

India continues to be a write-off, both financially and politically.

Russia is slowly becoming more capitalistic, as the U.S. has become less so. Both are gradual processes with much farther to go before they can be said to be completely altered. Russian military might is easily now the dominant one in the world. This is causing considerable worry in Europe and China. A China-Russia war seems inevitable. Europe has finally begun to re-arm in earnest.

IS THIS PROGRESS?

If we had foreseen all this in 1973 I think some would have committed suicide, and yet life goes on, and really isn't as bad as it might have sounded as a prediction. A very elderly friend of mine just before he died in 1973 said to me "When I was a boy in 1890 and America was free and capitalist, and the American ideal was still eagerly pursued, if somebody could have shown me the havoc socialism would have wrought on the country I would never have wanted to see manhood." I wondered what he meant, for while I saw impending money disaster, I had to admit that the world had never been more materially prosperous, and there were a number of good things about the prior two decades. Now I know what he meant. The world goes on and *values* change, and nothing is wholly bad. Man is an incurable optimist, and he *has* to believe that each year is in some ways better than the last, otherwise he would not reach for the stars and make progress which somehow on balance he does.

This current situation could go on for decades more. Sure, many of the things we were afraid of a decade ago HAVE been solved and the world is a better place. The fear of *pollution* is gone, though not because it became an ideological issue that everybody rallied behind. Much more practical than that. Car manufacturers couldn't be forced to make a nongasoline car for *humanity's* sake, but they very soon came up with it when the Arabs made the gas engine cease to be viable on an economic basis. When they rationed gasoline and oil and the price rose out of everybody's reach, then suddenly the car manufacturers HAD to come up with an alternative or go out of business—and they did, in 12 months flat. So the Arabs, not the conservationists, solved our pollution problem for us, and the other aspects of pollution are also well on the way to being solved. After that awful cholera epidemic that killed so many people in 1978, which was simply caused through inefficiently recycled water, suddenly something *had* to be done. When 2000 people died in New York City in four days then action *WAS* taken, just as London kicked its smog problem after a bad smog which killed thousands back in the 1950's.

We aren't getting overpopulated either. People don't seem to be *having* children anymore. In fact the latest government discussions are on whether to up the family allowances plan which was brought in, in 1980, to persuade people to have families. They want to double the allowance of Social Security paid to families with more than two children. In 1973 I never would have believed that America would *pay* people to have children, and pay them no matter

what their income level was. But the world changes and we adjust.

VOTING WITH THEIR FEET

The exodus of Americans out of the U.S. continued its speed-up and today there are an estimated 10 million Americans living abroad. You see lots of ads trying to entice Americans back to the U.S. to accept high paying jobs, the same as one used to see from underdeveloped countries 10 to 15 years ago. The people to leave an eroding country are always, throughout history, the most skilled: the doctors, intellectuals, artists, writers, etc.

Oh, and Mike Oliver finally got a new nation started. It began humbly in 1975 and now has a population of 175,000. Yet it has issued 4,000,000 passports to its mostly nonresident citizens, none of whom need pay tax of any kind. The new nation has the hardest currency in the world.

"Happiness comes from making one's future secure through being an island, self-sustaining, strong, confident, and relatively safe."

By the way, Paul Adolf Volcker was asked in 1974 to move from the Treasury to the U.S. Department of Agriculture, because, it is rumored, of tremendous pressure from Congressmen and conservatives throughout the U.S.A. He is now in charge of compiling international statistics on insecticides and fertilizers.

Silver, by the way, also rose, pretty much in proportion to gold, in terms of the dollar.

Yes, overall life is tolerable. More so in some parts of the world than others, to be sure. I worry a bit about France. Since her attempted coup and the collapse of her currency, her government has taken on more and more power. She is the nearest thing to a dictatorship on the continent of Europe. If things ever blew up, they could start there. France also has funny alliances with Russia, China and the Middle-East. But this is speculation. I would say, as I stand in 1985, World War III is possibly five years away, at least, if it ever happens. Wars don't explode from nothing; they start as a trickle, and then get bigger. The world is full of small streams that could increase, but these take time, and I am not predicting, merely looking back.

THE MORE THINGS CHANGE . . .

Looking back over the past 12 years I'd say as I did in 1960, *"plus ca change, plus c'est la meme chose."* The more things change, the more they stay the same. We thought in 1973 that if we could get over this hurdle, get a good money system going, then the whole world would break forth in stability and prosperity. But typically man compromises. We got a better system in part of the world, in Europe, but a worse one in North and South America. It seems that after all, the main philosophy which I used to preach that has best stood the test of time is that you must look out for *yourself.* You must create your own world so to speak, and to do so requires the absence of preconceived notions, prejudices, bias, patriotic chains, or over-confidence.

I believe cynicism is the wisdom that comes with age. I'm 12 years older now, 12 years more cynical and I feel 50 years wiser for it. It's a *mixed* blessing perhaps, but still a blessing, to reach the conclusion one *is* alone in the world. It was comforting when one trusted to luck or faith or government or system. But it's far safer to know that you stand or fall from your own two feet and this way you face the problem squarely and deal with it realistically and are much more secure as a result of the effort you make. If happiness is a blanket of security then happiness comes from making one's future secure through being an island, self-sustaining, strong, confident, and relatively safe.

In English we have the phrase "every man for himself." In French they say "sauve qui peut" which translates into "save himself who can."

I hope this trip in my time machine will help someone save himself after seeing the potential of the future. ◻

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Congress shall make no law restricting the freedom of wages and prices nor authorizing commodity allocations. The right of citizens to make contracts and to trade freely among themselves shall not be abridged.

SECTION 2. **Monetary Policy**

It shall be the policy of the Treasury of the United States to stabilize the supply of cash notes and Federal credit in circulation, and thereby to preserve and increase the purchasing power of the currency of the United States.

SECTION 3. **Fiscal Policy**

On the fourth day of July in the year following the year of ratification of this article, the sixteenth article of amendment to the Constitution of the United States shall be repealed. A levy of taxation sufficient to discharge the financial obligations of the Federal government shall be apportioned among the several States by Congress annually as the first act of each session, but the power of direct taxation shall be reserved to the several States. Congress shall not impose any tax on the property or income of citizens of the United States, nor shall any internal revenue service be maintained.

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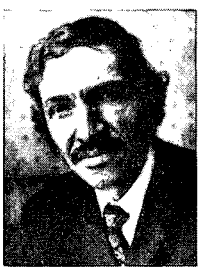

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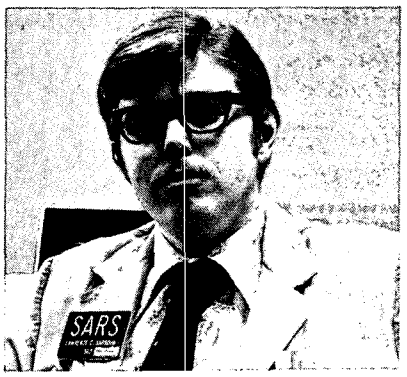
A Primer on Foreign Currency Trading

Lawrence Sarsoun

Foreign exchange is the currency of nations other than one's own and includes in its definition the process of transactions transferring ownership of one currency to another.

The history of foreign exchange dealings begins in ancient times. In medieval times, the European trade fairs began to draw participants from various nations. Most fairs would find a broker willing to buy and sell the various currencies at varying rates usually dependent on the simple law of supply and demand, flavored with a little of the "whatever the traffic will bear." Another novel and interesting idea was also being brought to fruition at these meetings—the idea of a futures contract, a commitment to buy or sell a commodity at some time in the future—in this case, upon the occasion of the next fair. This idea lent itself equally well to the business of dealing in foreign exchange and thus was born the forward or futures market in foreign exchange.

The job of effecting these transactions fell to those institutions capable of holding and handling large sums of money, the banking community. The banking business, however, realized the necessity and advantage of having an anonymous middleman to handle the transaction. So the trading of foreign exchange by banks came to be handled by a number of *forex* (foreign exchange) *brokers.* Each major financial center has its brokers and banks all dealing forex by phone or by cable.



Lawrence C. Sarsoun began his career in finance in 1960. In 1966 he published his first manual on commodity trading and began writing a weekly analysis of the egg futures market for Hayden Stone, Inc. In 1972, he became a member of the International Monetary Market and was made manager of Heinold Commodities' IMM division. He has authored the "Foreign Currency Futures Handbook" and produces a weekly newsletter on the IMM and foreign exchange markets.

There are a few exceptions, such as in Europe, where centralized market places are also used. In the United States, the International Monetary Market (IMM) in Chicago is a centralized public foreign exchange market.

The market price for one currency denominated in terms of the currency of another nation has been derived by various means over the past 100 years. We will briefly cover some of the various systems used.

In the 19th century, currencies of most countries were backed by a monetary metal, either gold or silver, or in some cases, both. These metals were used as backing because they represented "store of value" money; i.e., the commodity metal was relatively difficult to procure and its scarcity maintained its value at relatively stable rates. This stability of the monetary metal lent stability to the currency it backed. The occasion of new finds of gold and/or silver were generally the only threat to the stability of the reserve metal.

The value of almost any currency could therefore be expressed in terms of a quantity of the metal or in terms of another currency whose value was denominated in terms of the monetary metal. A country was said to be on the "gold standard," "silver standard," or using a "bimetallic standard." Rates of foreign exchange were relatively stable until various economic pressures (to be discussed in detail later) brought about an adjustment of the rates between one currency and another.

The gold standard dominated the world throughout the late 19th century but was suspended during the First World War as nations resorted to embargoing gold. War costs were financed by the printing of fiat money and efforts to restore the gold standard after World War I laid the seeds for the depression of the thirties. Germany underwent a massive printing press inflation which saw the foreign exchange value of the postwar reichsmark fall to almost nothing. France, dependent on German reparations payments to pay off war debts, also suffered a decline in the value of the franc.

During the depression, with its concommitant deflation in prices, President Roosevelt strived to help domestic farmers by devaluing (see definitions) the dollar. The dollar had previously been expressed as 1/22 of an ounce of gold (i.e., one ounce of gold cost $22.00). Roosevelt changed the gold value of the dollar to $35.00 an ounce. The intended effect was to make American agricultural products more competitively priced in world markets and thus increase exports of such products. Helping the farmer was expected to be the first step in getting the economy going again. The result was a world-wide flurry of competitive devaluations as each country sought to derive an advantage over its trading partners through a change in the exchange value of its currency. Years later, the American President was to find that exporting men and war machines had a more profound effect.

During the latter part of World War II, financial leaders of the world met at Bretton Woods, New Hampshire to work out a new monetary system. Based on the U.S. dollar, the system allowed for convertibility of currencies into gold via the dollar. All currencies were thus indirectly convertible to gold. The U.S. agreed to buy and sell gold to foreign central banks (only) at $35 an ounce, plus or minus a small service charge. The exchange rate of all other currencies were then denominated in dollars at certain fixed rates. A variation in the exchange rate of plus or minus one percent adjustment was allowed to compensate for economic variables, such as balance of trade and balance of payments deficits or surpluses. The system was based on the newly established power of the United States and the U.S. dollar and was to last for over 27 years.

Under the Bretton Woods agreement, if, for example, the Swiss franc central rate was $.23, the SwF would be allowed to fluctuate from $.2277 to $.2323, a one percent variation either side of the central rate. If the Swiss were experiencing difficulty in their balance of payments, it might be that the exchange rate for Swiss francs would decline in dollar terms. In other words, there would be less demand for SwF and the dollar cost would decline. If it declined to $.2277, then the central banks would intervene in the foreign exchange market, selling foreign exchange and buying Swiss francs in order to prop up its exchange value.

Conversely if the Swiss economy were strong while the U.S. economy was weak (relatively), then the dollar cost to buy SwF could conceivably move to the upper end of the intervention band. In that instance, the U.S. dollar would be supported and SwF sold at the $.2323 level.

If economic pressures were significant, and intervention failed to have the desired result, then a major readjustment of the central rate would be made.

If, as in the first example, it were the Swiss economy in trouble, the rate for SwF might be lowered in dollar terms, say to $.20. This would be a *devaluation* of the franc and a *revaluation* of the dollar. In the second example, the adjustment of the Swiss franc in dollar terms from $.23 to $.26 was a *revaluation* of the SwF and a *devaluation* of the dollar.

DEMISE OF BRETTON WOODS

At its inception in 1944, the Bretton Woods agreement found the United States dollar liabilities roughly in balance with its reserves. Throughout the fifties and sixties, however, American foreign aid generally outpaced the growth in reserves. Since 1950 (excepting 1958) the U.S. has run payments deficits (see *balance of payments* under Definitions) every year up to and including the present. 1959 saw the growth of foreign liabilities begin to outrun reserves at a quickening pace. In later years, the gold reserve requirement would be lowered from 40 percent to 25 percent, and finally removed completely. The U.S. and thus the world was moving from a dollar-exchange system to a fiat money system. During the sixties, foreign nations began to ask for gold in exchange for their dollar holdings. Our gold reserves dropped from a high of $24 billion in 1958 to a low of $10 billion in 1970. The U.S. continued to expand its money supply and inflation brought with it the specter of a depreciating dollar.

Efforts to restore stability in 1967 through the formation of a gold pool and a two-tier system for the price of gold managed to buy some time but ultimately dissolved in failure. The U.S. was forced to close the gold window and would not exchange gold for dollars. The dollar was no longer as good as gold.

Ultimately the U.S. was forced, by continuing huge payments deficits and indeed even a trade deficit (the first in over 70 years), to devalue the dollar in terms of gold. The Bretton Woods system

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DEFINITIONS

Appreciation—A rise in the value of a currency in terms of foreign currencies.

Arbitrage—The simultaneous buying and selling of foreign exchange for the sake of realizing profits from discrepancies between exchange rates prevailing at the same time in different centers, or between forward margins for different maturities, or between interest rates prevailing at the time in different centers or in different currencies.

Band—The allowable range of exchange rates above and below parity (or the central bank rates).

Balance of payments—Surplus or deficit on total current and external payments and long-term capital movements settled by a change in short-term capital movements.

£—British pound

Bear—A speculator going short in anticipation of a depreciation.

Blocked accounts—Nonresident funds

Bull—A speculator going long in anticipation of an appreciation.

Can$—Canadian dollar

Central bank—The national or government bank of a country.

Closing out—The offsetting of a futures position.

CME—The Chicago Mercantile Exchange.

Convertibility—The right of holders of a currency to transfer their funds into another currency or gold.

Deflation—A constriction of the money supply with the result that prices tend to decline.

Depreciation—A decline in the gold value or exchange value of a currency.

Devaluation—A downward change in the official parity of an exchange, or of an exchange rate at which it had been pegged for some time.

Devaluation prone—A currency which is widely expected to be devalued.

Discount—Spot exchange inferior to parity is at a discount. Futures that are cheaper than spot are said to be at a discount.

DM—Deutschemark

Euro-dollars—Time deposits in terms of dollars lent and borrowed in financial centers outside the U.S.

Forward exchange—Futures

Futures—The system or process of operating in foreign exchange for future delivery.

G.N.P.—Gross national product.

Gold standard—System under which the international value of a currency is kept stable in terms of gold and in terms of other currencies based on gold by means of its free convertibility into gold.

Hedge—Foreign exchange (spot or futures) or foreign borrowing operations to safeguard indefinite and indirect exchange risk arising from assets or liabilities whose value is apt to be affected by changes in exchange rates.

IMM—The International Monetary Market of the Chicago Mercantile Exchange.

Inflating—Expansion of the money supply without a corresponding and equal increase in reserve backing (gold) or in goods and services.

Leads and lags—In this manuever, importers may slow payment to countries whose currency is devaluation-prone and speed payment to a country whose currency is revaluation prone.

Long—Having bought, one is said to be long.

Mex$—Mexican peso

Parity (par value)—The value of a currency in terms of the U.S. dollar or a fixed quantity of gold.

Premium—Value of spot exchange in excess of parity. In relation to futures, it means that the currency is dearer for future delivery than for immediate (spot) delivery.

Revaluation—Upward change in the official parity or in the exchange rate at which an exchange was pegged.

SwF—Swiss franc

Short—Having sold, one is said to be short.

Speculation—Creation and maintenance of uncovered positions (outright long or short) in foreign currencies (either spot or futures) for the sake of prospects of making a profit through a change in the exchange rate.

Spot rate—The current cash market quote for foreign exchange.

Swap transactions—This is the purchase of spot exchanges against the sale of futures.

¥—Japanese yen

would be quietly laid to rest and a new system, The Smithsonian Agreement, would restore monetary stability to the world. But it never did.

The Smithsonian was put together with a new set of central bank rates and a wider intervention band of 2¼ percent above or below the central rate, and a new gold price of $38.00. It was to last less than a year. At the same time that the world was opting for a 4½ percent band, the European economic community (EC) elected to keep their currencies with a narrower band of 2¼ percent (plus or minus 1-1/8 percent) vis-a-vis each other.

While the United Kingdom (UK) unofficially tried to maintain itself within the EC band (which came to be known as the European Snake) the sterling-dollar central rate appeared to have been misconceived at $2.60 per £. In June 1972, after a brief attempt at intervention, the Bank of England allowed sterling to float. The pound quickly sank, like a rock, from $2.60 to $2.42. Sterling has floated ever since, bobbing on the monetary sea, from $2.42 to $2.52, sinking to $2.32, rising to $2.35 and of late, sinking again, this time to $2.1750.

Later that same year, the rush to dispose of inconvertible dollars into more stable currencies would bring about pressure on the European nations and Japan to repeg their rates to the dollar at new levels. The Swiss franc and mark revaluations (see definitions) occurred in the fall and marked the beginning of the end for the Smithsonian. Death occurred at the occasion of the second U.S. dollar devaluation in February 1973. At that time, the currencies of most major nations were floating; i.e., while central bank rates were still defined, there was no longer any formal agreement to intervene, vis-a-vis the dollar, at some specified level. Instead informal intervention might occur at some arbitrary rate, decided, oft times unilaterally, by the central bank of a nation. This was referred to as a "dirty float." The EC Snake, however, was restructured and the Europeans continued to maintain their rates vis-a-vis each other, intervening and revaluing or devaluing as might be required. The exceptions were the pound sterling, which still floats, and the Italian Lira, which is a two-tier float. Other EC nations also have two-tier currencies.

SOME FUNDAMENTALS OF FOREIGN EXCHANGE

All of the above movement in exchange rates has occurred in the various world markets for foreign exchange in response to economic functions. These fundamentals include trade balances, political and social factors, government budgets and expenditures (fiscal policy), money supply and interest rates (monetary policy), and payments balances (trade and capital surpluses or deficits combined). In noncrisis periods, the most sensitive fundamental is that of interest rates, as these affect the flow of funds from country to country, seeking the highest return. Expectations of changes in direction (anticipation) also affect the market both in spot and forward dealings. For example, if the British pound sterling were under speculative selling pressure because of social unrest, labor strikes, and concurrent terrorist attacks, one might anticipate that the Bank of England minimum lending rate would be increased a percentage or so in order to attract sufficient inflow of funds, seeking the high interest, to offset the outflows attributable to the bearish fundamentals. However, boosting the interest rate will only firm the spot. Forwards will decline under the speculative pressure as well as forward hedge selling by those moving into British debt instruments.

As another example of interest rate functions of spot and forward exchange, the Mexican peso forward market has always been at a discount to spot because Mexican financiera note yields are significantly higher than U.S. rates. Investors buy spot pesos, invest in the financieras at 10-11 percent per annum, and then look to hedge their investment and return by selling in the forward market in order to cover their exchange risk. If the discount is only 1—2 percent, then the hedge investment will return 8—10 percent. If the discount is greater, then the investor may be reluctant to invest in an unhedged instrument. Barring expectations of a Mexican peso devaluation, forwards would then rise to the level of a 1—2 percent discount.

During the monetary crisis of 1971-73 when speculation against the U.S. dollar caused inflows of capital into Swiss francs, deutsche marks, and Japanese yen, these countries reduced their interest rates to very low levels (Switzerland even went to a negative rate) in order to discourage such inflows. Under normal circumstances, if another country had a lower interest rate than the U.S., then forwards for those currencies ought to be at a premium to the spot quotation.

ANALYZING THE FUNDAMENTALS

Proper analysis of the fundamentals is a necessary prerequisite for the speculator in foreign exchange. What is less widely understood is the need for importers, exporters, and corporate treasurers of multinational concerns to include fundamental analysis in their planning. Product pricing without consideration of the exchange risk can result in what was originally a profitable deal becoming less profitable or not profitable at all.

The first fundamental of importance is interest rates. However, the impact of interest rates on exchange rates is most significant *only* in times of normalcy. In other words, in times of monetary crisis, interest rates assume less significance.

Of further importance are the balance of trade, capital flows, balance of payments, G.N.P., government budgets, fiscal and monetary policy, and monetary reserves. Let us review each to see how they affect exchange rates.

Balance of Trade—If a country imports more than it exports, then there will be a net outflow of its currency. As the supply of its currency increases, the value will decrease, as in any other supply and demand situation. If a country is a net exporter of goods, there will be demand for its currency to pay for its goods. Germany and Japan are good examples of this latter case, running up large trade surpluses for many years.

Capital Flows—If a country is a net importer of capital it will have a capital flows surplus. Oft times, a nation that is a net importer on trade (a balance of trade deficit—capital flowing out in payment) will have investment capital flowing in to balance the trade deficit. If one balances the other, then this would make for a balance in the overall account of the country, which final figure is referred to as the balance of payments.

The balance of payments, which is roughly the trade deficit or surplus and the capital flow deficit or surplus added together, indicates the financial standing of a country. It is a key factor in the stability of the exchange rate. The U.S., for example, ran balance of payments deficits for years and was finally forced to devalue. Running capital flow deficits for years (and even a trade deficit in 1972) caused a loss of monetary reserve in the form of gold. When our reserves of gold had been drawn down to a level considered minimal for military protection, the outflow of gold reserves ceased and the dollar was devalued. Similarly, in the case of Japan, its history during the sixties had been one of trade surpluses, increasing reserves, and an eventual revaluation. After the two devaluations, Japan took its reserves, which consisted mainly of American dollars, and used these reserves for purchases of goods, such as American soybeans and pork (which caused a decline in their trade surplus), and used reserves for capital investment, such as buying the State of Hawaii, parts of California, and American stocks and companies. This caused a huge loss of reserves and a balance of payments deficit, which in turn, necessitated a depreciation of the yen. Currently, because of the oil crisis, Japan and Germany, for

example, will be faced with higher energy costs. This will, in turn, cause higher import prices and will cause the balance of trade to decline to a smaller surplus, or even to a deficit, and will adversely affect their reserves. In order to retain reserves and remain competitive in world markets, these countries would be willing to devalue their currencies. The net result of higher oil prices will be a world-wide balance of payments deficit by the industrial oil-using nations and conversely, huge balance of payments surpluses by the oil-producing nations. The oil users will resort to competitive devaluations to offset the higher oil prices and save reserves. After a while, it will be the Arabs buying Hawaii from the Japanese!

Gross National Product—If a country were to increase its productivity, then it should be expected that its goods would become more competitive in world markets and its balance of trade and payments improve.

Government Budgets—Fiscal policy can affect exchange rates insofar as the funding of government expenditures has an effect on the domestic economy. Raising taxes to pay for government spending decreases spending in the private sector while monetization of the debt by inflating the money supply increases the likelihood of higher prices and diminishes the probability of good trade figures.

Monetary Policy—Attempts to improve a country's external account are usually done at the expense of its domestic economy. For example, if interest rates are raised in an effort to encourage capital inflows and stabilize the exchange rate, it will also have the effect of slowing down business domestically. Declining business activity will lower prices until such times as they become attractive in world markets. World demand improves the trade figures; business activity increases again and the cycle goes on.

Monetary policy includes the utilization of changes in the discount rate and expansion or contraction of the money supply.

SUMMING UP THE FUNDAMENTALS

In review, individuals should keep abreast of the following statistics and review the *relative* difference between them in order to assess possible exchange rate changes:

General
- Interest Rates
- Money Supply
- Monetary Reserves

Domestic Account
- Wholesale Price
- Consumer Prices
- Gross National Product
- Government Spending

External Account
- Balance of Trade
- Capital Flows
- Balance of Payments

Spot— Jan. 28		Bid $.2950	Offer .2955	Actual Price Bid	Offer
1 month	(30 days) Feb. 26	+ 2 + 4	=	.2952 -	.2959
2 months	(60 days) March 28	Flat +2	=	.2950 -	.2957
3 months	(90 days) April 26*	- 4 - 2	=	.2946 -	.2953
6 months	(180 days) July 26	- 10 - 5	=	.2940 -	.2950
12 months	(360 days) Jan. 28	-20 - 15	=	.2930 -	.2940

*April 27, 1974 is a Saturday. If value date falls on Sunday, value date becomes the following Monday. If Saturday, the value becomes the preceding Friday.

UNDERSTANDING THE QUOTATIONS

The cost of one currency in terms of another is referred to as the exchange rate. The rate can be expressed in terms of either currency. On the IMM and in U.S. forex markets, foreign currency is generally denominated in U.S. dollar terms. For example, a recent quote for British pounds was $2.1790–$2.1800. This meant it cost $2.18 to exchange (purchase) one British pound while one could sell one British pound and receive $2.1790.

Likewise, the quote for one German mark (deutsche mark) was $.3500–$.3510. In other words, if you were purchasing DM's, you would pay 35 and 10/100th cents per DM. If selling DM's, you would receive 35¢ for each. Similar recent quotes for IMM currencies are as follows:

- Swiss Francs = $.2950 (29½ cents per SwF)
- Dutch Guilders = $.3300 (33 cents per f.)
- Japanese Yen = $.0033300 (1/3 cent per yen)
- Canadian Dollar = $1.00800 (one dollar and 8/10th of one cent per Canadian dollar)
- Mexican Peso = $.08006 (eight and 6/10000ths cents per Mex $)

Likewise, the above exchange rates can be quoted in terms of the other currency. This is referred to as the reciprocal. For example:

- $.0033300 to the yen = 300 yen to the dollar
- $.08006 to the peso = 12.49 Mexican pesos to the dollar
- $.2950 to the SwF = 3.3890 Swiss francs to the dollar
- $.3500 to the DM = 2.8570 deutsche marks to the dollar
- $.3300 to the f. = 3.030 guilders to the dollar

Transactions in forex fall into two categories, those for immediate delivery (spot) and those for delivery at some time in the future (forwards). In actuality, spot transactions involve a one day delay for North American currencies and a two day delay for EC currencies and the Japanese yen. For example, spot Canada or Mexican peso quoted today is for delivery the next business day while spot today for DM, SwF, guilders, £, and yen is for delivery two business days hence. This delay reflects the time needed to effect cable transfers and handle the necessary paperwork. Quotations for forwards are expressed in terms of a discount or premium to spot.

Example: Today is Thursday, January 24, 1974. The value date for spot Swiss francs would be Monday, January 28. Forwards are quoted for 1, 2, 3, 6, and 12 months forward, in 30 day increments.

The bank forward market is therefore primarily dealing on a monthly basis from

Contract Information of Currency on the IMM

	Size of Contract	Recent Spot	Contract Value in $'s	Margin	Margin as % of Value
British Pound	£ 25,000	$2.18	$54,500.00	$2,000	3.6%
Canadian Dollar	Can$ $100,000	$1.00800	$100,800.00	$1,500	1.5%
Dutch Guilder	f. 125,000	$.33	$41,250.00	$1,500	3.6%
Deutschemark	DM 250,000	$.35	$87,500.00	$4,000	4.5%
Japanese Yen	¥ 12,500,000	$.0033300	$41,625.00	$1,500	3.6%
Mexican Peso	Mex$ 1,000,000	$.08002	$80,002.00	$1,500	1.9%
Swiss Franc	SwF 250,000	$.2950	$73,750.00	$4,000	5.4%

A TRADING EXAMPLE
December 1, 1973

Speculator

John Doe, a speculator, has, after much research and analysis, decided that the exchange rate of the Swiss franc may move higher from its present levels, over the next six months. Realizing also that he may be wrong, Doe uses only risk capital, money that he can afford to lose. He establishes a profit objective *and* a loss factor, at which point he will sell his position. He contacts his broker, puts up margin, and puts in an order to buy June Swiss Francs at current levels.

Hedger (Sell Hedge)

The XYZ Co., a multinational corporation with a subsidiary in Switzerland, needs to fund operations for the subsidiary for the last six months of its fiscal year, ending in June of 1974. In December of 1973, XYZ purchased 500,000 Swiss francs at $.29600 for a dollar outlay of $148,000. Concurrently it sold 2 contracts (SwF250,000x2=SwF500,000) of June SwF at $.29500 to protect against the exchange risk. It did this by (1) contacting an IMM broker, (2) filling out routine customer forms, (3) depositing margin ($4000x2=$8000), and (4) entering the order on the IMM.

TRANSACTION

Speculator	Hedger
Buys 2 June SwF $.29500	Sells 2 June SwF $.29500

John Doe has correctly assessed the firming of the SwF and on June 1, is able to liquidate his long position in June SwF at $.30090. His return is 590 points x 5 = $2950 minus a $45 commission fee, netting him $2905.

At this time, XYZ's Swiss subsidiary sells the SwF 500,000 in the spot market and buys in the futures market. If spot were $.30100, its return in cash would be $150,500 less $148,000 = +$2,500. Assume the June SwF had risen to $.30090 (almost to spot). The offset in futures would cost XYZ $2950 plus a commission fee of $45 = $2995 less the gain on the cash position of $2500 = a net hedge cost of $495. If the exchange rate had declined during the period the loss on cash would be offset by the gain on future.

TRANSACTION

Speculator	Hedger
Sells 2 June SwF $.30090	Buys 2 June SwF $.30090

TRADING EXAMPLE #2
December, 1973

Hedger (Buying Hedge)

ABC, a multinational company, has a Swiss subsidiary with excess funds while its domestic operation is in need of short term funds for operating expenses. ABC would sell SwF in the cash (spot) market and buy futures.

Cash

Sells 500,000 SwF @ $.29600 = $148,000

Speculator

John Smith, a speculator, has, after much research and analysis, decided that the exchange rate of the SwF may move lower from its present level over the next six months. Realizing also that he may be wrong, Smith uses only risk capital, money that he can afford to lose. He contacts his broker, puts up margin, and places an order to sell June Swiss francs.

Futures December, 1973

Hedger	Speculator
Buys 2 contracts June SwF @ $.29500	Sells 2 contracts June SwF @ $.29500

In June, ABC would buy SwF 500,000 in the spot market (assuming a spot of $.30100 = $150,000 a loss of =$2500 and would sell 2 June SwF in the futures market for a gain on futures of $2950 minus $45 commission, minus $2500 loss in cash for a net gain of $405 on a buy hedge.

If the market had gone against Smith, then he would be required to maintain his margin in the account. Assuming a rise in SwF to $.30090 by June, Smith would have a loss of $2950 plus a commission of $45 for a loss of $2995.

Futures June 1, 1974

Hedger	Speculator
Sells 2 June SwF $.30090	Buys 2 June SwF $.30090

the spot value date. The IMM uses a different system. Contracts are standardized, with the value date being the third Wednesday of the month, on a quarterly basis. For example:

1974	March	March 20
	June	June 19
	Sep.	Sept. 18
	Dec.	Dec. 18
1975	March	March 19
	June	June 18

THE FUNCTION OF THE ARBITRAGEUR

It is at this point that the arbitrageur enters the picture. He is the conduit between the inter-bank market and the IMM. The arbitrageur takes the bank rate for the day and interpolates the forward swap for the value dates used on the IMM. In this manner, he can bid or offer on the IMM at a few points difference from where the bank will deal. The IMM is therefore always relatively close to rates in the international forex bank market. For example, if the arbitrageur were making a market on the IMM for the June Swiss franc he would take the three month forward swap -4-2 and the six month -10-5 and would compute for his value date, June 19. The difference between the three and six month bids is -6 (-4=10=6). June 26 is 60 days beyond the three month so June 19 is 60 minus 7 = 53. There are 90 days between the three and six months so June 19 bid is 53/90ths of -6. This sum, 3.53, is added to -4 to equal -7.5. The offer side for June 19 is 53/90ths of -3 added to -2 or 3.7. Therefore:

Spot	.2950-55	Bid	Offer
June 19	-7.5 -3.5 =	.29425	- .29515

The arbitrageur on the IMM would bid at a price below .29425 and offer above .29515. If his bid is hit, he will immediately sell a like quantity of this same value with his bank. Competition between arbitrageurs will, in time, make their rates very close to the bank rate. If a public market such as the IMM develops a wide participation (as is happening) rates will equal or better those of the bank market, and will eliminate the arbitrageur completely.

It can be seen then that analysis of fundamentals in foreign exchange as an indication of exchange rate direction must also be modified by the application of information derived. The response of a speculator and hedger to sundry indicators may vary each according to his needs.

As in any other marketplace, supply and demand are determined by complex subjective factors, to best serve the needs of each trader. Hopefully, this article has succeeded in removing the mystery from the foreign currency marketplace. ◻

THERE'S MORE TO FREEDOM THAN SLOGANS

Everybody claims to be in favor of "freedom." Yet how many people really understand what it's all about? Consider the businessman who's all for free competition . . . unless his competition is named IBM or is Japanese. Or the mayor who wants plentiful transportation . . . but outlaws jitneys. Or the military leader who wants to defend freedom . . . using conscripted labor. Or the citizen who's all for free speech and press . . . so long as the material isn't "obscene." Each wants freedom for the things he considers important, but at the expense of somebody else's freedom.

At REASON Magazine, we believe in freedom for *everyone.* With Herbert Spencer and John Stuart Mill, we believe a person should be free to take any action, so long as it does not interfere with the liberty of anyone else. We call this point of view *libertarianism.* It is unabashedly individualistic, capitalistic, and (we think) reasonable. Moreover, this voluntaristic, free market approach points the way toward solutions to many of the problems created by the unbridled growth of Big Brother statism — like war, taxation, the energy crisis, and inflation.

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Foreign Tax Havens

Wainright Dawson, Jr.

A few hundred years ago, Ben Franklin began the search for the true tax haven. Said Franklin: "Where there is liberty, there is my country." Today, there are so many evolving and devolving tax havens, that Franklin might be moved to say, "If I can find some consistent liberty, that's where I'll put my money."

Perhaps when Americans finally do not have Richard Nixon to kick them around any longer, it will be easier to gain a valid perspective of just how much personal and financial liberty we have left. But for now, the emotional and financial search for "havens" of all kinds is intensifying.

Because of the U.S.-sponsored world-wide inflation, every haven is having problems with its currency and must make constant adjustments to the rules. This causes much difficulty as today's haven might become tomorrow's problem. But on the positive side, all this action is tending to create new avenues of financial expression faster than before. This means that selecting a tax haven is as specialized a process as selecting a home, car or anything else fitted to your taste and financial situation. Variety has advantages, but it takes longer to find the facts and decide.

First, all havens must be considered in light of the type of income you have, and expect to have. Second, all havens must be considered in light of the taxation laws of *your own country.* Third, consider the political and social aspects along with the financial when locating your haven. All too often one locates the "ideal" tax haven, only to discover language and/or cultural problems. Much upset and frustration can be experienced when life-styles bother you and local mores offend you.

Following that warning, we can proceed to your basic consideration: is the haven for investment or company business? Most legal systems allow the investor the greatest latitude in financial dealings. This is usually in the form of trusts. Companies formed abroad often find it to their advantage to engage in business with a foreign company on a 50-50 basis. In this way, income can be taxed only when repatriated.

In any event, here is a check-list of items to use for basic analysis:

- Political and economic stability
- Attitude of the country toward tax haven business
- Other possible taxes and fees (death duties, inheritance tax, etc.)
- Tax treaties (existing, possible, etc.)
- Exchange controls on currency; good havens have none
- Ability to conduct your business within the country
- Ease of forming a company (attorneys, costs)
- Systems of law (civil, common, ?)
- Transportation (accessible as you might require ?)
- Banking and communications facilities
- Political situation now, long term trends —will they change the rules?

When analyzing from tax considerations alone, there are four general classifications:

1. Traditional tax havens with no taxes at all, or so minimal as to be of no consequence such as: Bahamas, Bermuda, Cayman Islands, Liechtenstein.
2. Havens which impose taxes but at low rates, such as the British Virgin Islands and the Channel Island of Jersey.
3. Tax havens which tax domestic income but exempt all foreign sources, such as Hong Kong, Liberia and Panama.
4. Countries which allow special privileges but are not true tax havens, such as Luxembourg and The Netherlands. They are useful for holding companies only.

In actual practice, most any country can be a haven of some kind. Miami, Florida banks have created secret accounts for Cubans—for obvious reasons. The U.S.A. is also a tax haven for many foreigners in high-tax countries who can utilize our capital gains taxation.

A U.S. citizen may set up a company in England and have it classified as "nonresident" for tax benefits. For years, Puerto Rico has had fine incentives for businesses locating there. Ireland continues to grant tax holidays until 1999 for new companies bringing jobs, etc. This privilege, incidentally, has recently been reaffirmed after the mining industry was threatened with loss of this status.

Creation of a tax haven is not always the direct decision of a single government. In 1972 for instance, economic conditions forced the British to float the exchange rate of the pound and thereby to dismantle the currency controls of what was known as the "Sterling Area." The "Area" still exists, consisting of Ireland, Jersey, Guernsey, Isle of Man, and Sark. But the action freed many members of the Commonwealth from the currency controls and thus allowed them to develop more toward tax-haven status.

This, along with improved communica-

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tions, gave the Cayman Islands a great boost as a haven. Also about this time they secured more independent political status from Britain. The Caymans, of course, are the "in" haven these days because they:

- Have no tax treaties
- Are English speaking
- Have stable government
- Permit companies to be easily formed, inexpensively (trusts also)
- Have good air transportation (until energy crises became more frequent)
- Have offices of most major banking institutions
- Have a system of company law that is sound and carefully developed

But just to show that all is not perfect, problems may develop in the Caymans in these ways:

- Imported foreign labor is tending to upset social stability
- Resources are limited, as is land; all prices are rising
- Most "tourism" is, in effect, controlled by the U.S. and before long treaties on taxation will be offered in a way that will be difficult to refuse
- U.S. tax law is being tightened to make problems for you in terms of what you do there

Of course, when treaties and new IRS rulings close liberty's doors, enterprising countries will come up with new free market conditions to offset the problems. This is a never ending game of "Follow the Legislation," but the advantages are usually worth it. Taking a look at some "old" and "new" tax havens will help explain this process. First a few of the "has-beens."

URUGUAY: long before all this became fashionable and really necessary, Uruguay was the Switzerland of South America. In the 1950's political stability was lost and the money moved out. Much of it went to—

MONACO: this principality still has some advantages, but in 1963 the French barred their citizens from individual and corporate business there. The resultant controls sent most other nationalities elsewhere, such as:

THE BAHAMAS: fine tax haven status was enjoyed until a recent change in government. Then restrictive residency requirements and increased taxes in certain areas sent thousands of companies and individuals to the Caymans. In the Bahamas' defense however, it should be noted that the residency restrictions have been eased a bit and the government has maintained most of the favorable tax advantages. Also, because of the exodus of capital, prices for businesses and real estate are bargains. Government policies bear watching, but the speculative situation is excellent.

All tax havens are in a state of flux, but a few bear mention as their recent progress has been very positive.

BAHRAIN: this island state in the Persian Gulf is increasing its banking and communications facilities rapidly. It is a major connection point for Middle East air transport.

BERMUDA: the closest and best for many categories, particularly trusts and holding companies. It is more difficult to get established here, but this, and the deliberate lack of publicity, are long-run advantages.

HONG KONG: has a wild stock market for the activists, bank secrecy, no currency controls, some local political problems, but still the best Asia has at present.

LIECHTENSTEIN: fine legal system, banking is Swiss in design and practice, currency is Swiss. In many ways this little country is the best of all. But you must really know what you want or you will be politely discouraged.

NEW HEBRIDES: these South Sea islands are increasing their services and facilities rapidly; distance and energy problems will slow progress.

SINGAPORE: this city state has been independent for a little over a year and has made the most of it, rapidly becoming the largest capital market in Asia. The Prime Minister is determined to make it the "Switzerland of the East."

But what of the real Switzerland? It is *not* a *tax* haven. It is a *money* haven, and still the best in the world. When a country has (as the Swiss just did) a national referendum and votes to continue strong anti-inflation policies, that country is to be respected —its laws and its currency.

If you make money in or, in most ways, through Switzerland, you can expect taxes to average 30 percent. However, for nonresident banking functions and some trust situations, taxes may be deferred until profits are claimed in your own country. The Swiss have tax treaties with the U.S. which can help you to avoid double taxation. The new, more famous, treaty is really so much propaganda by the U.S. Article 17 of that treaty insures the Swiss of their rights to interpret their own tax and bank law as they see fit. The treaty merely establishes some guidelines for communication and procedure.

An interesting working situation for favorable tax status combines the company law of Liechtenstein with the banking facilities of Switzerland—the better parts of two fine worlds of commerce.

Also in that part of the world is the developing importance of Austria. With a history of banking excellence that goes farther back than the Swiss, the new East-West ties are making this country an increasingly active center of finance. At present it is a good place to bank in any currency you prefer, and a nice place to vacation. Tax haven status is a way off as yet, but it bears watching.

Whatever your financial needs regarding tax havens, there are certainly one or two places that will interest you. If not, wait awhile and something is bound to turn up (if you don't create it yourself). As far as countries and legal/political systems are concerned, we live in an increasingly creative age. As always, political oppression is the mother of libertarian invention. ◻

For A New Country. . .

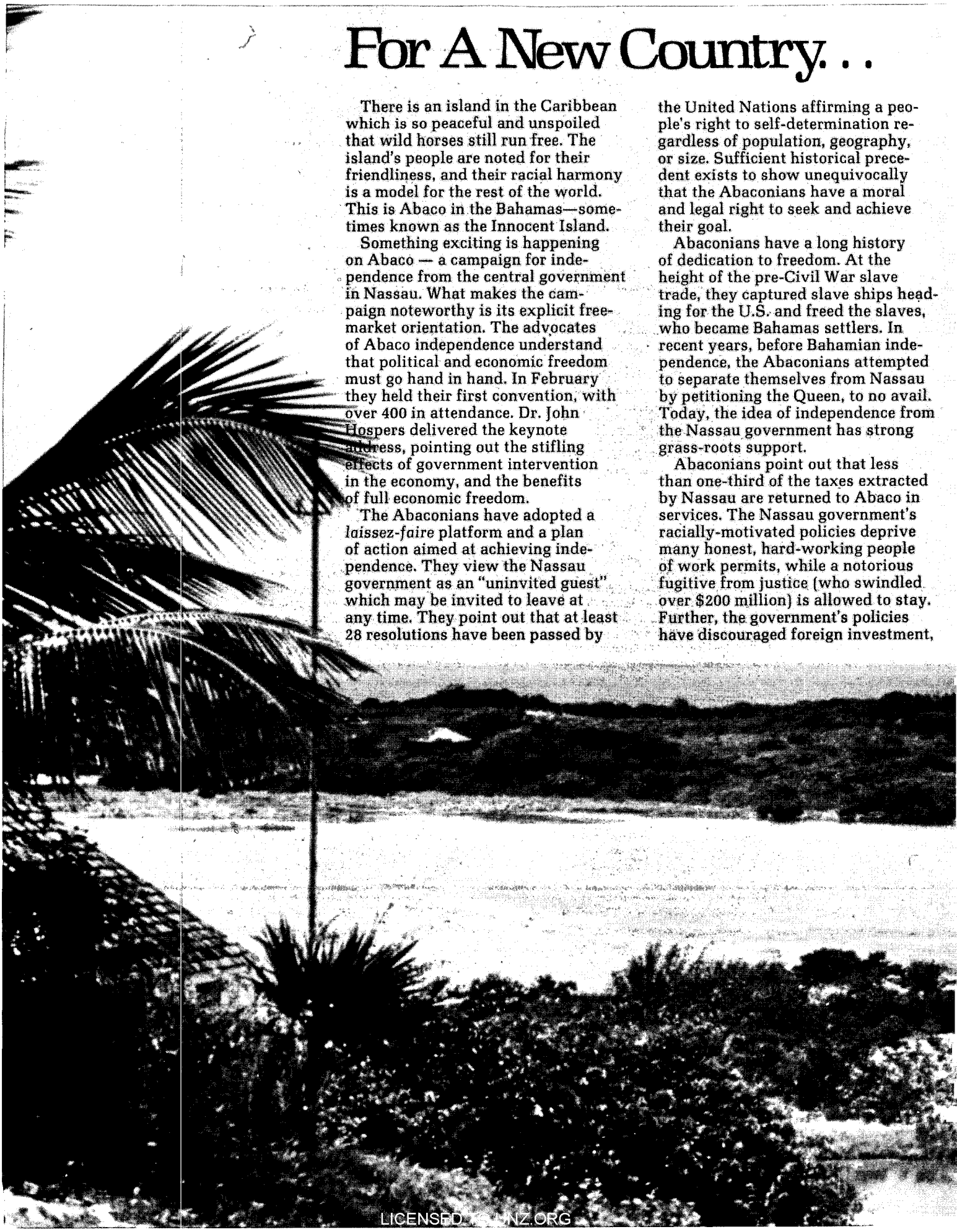
There is an island in the Caribbean which is so peaceful and unspoiled that wild horses still run free. The island's people are noted for their friendliness, and their racial harmony is a model for the rest of the world. This is Abaco in the Bahamas—sometimes known as the Innocent Island.

Something exciting is happening on Abaco — a campaign for independence from the central government in Nassau. What makes the campaign noteworthy is its explicit free-market orientation. The advocates of Abaco independence understand that political and economic freedom must go hand in hand. In February they held their first convention, with over 400 in attendance. Dr. John Hospers delivered the keynote address, pointing out the stifling effects of government intervention in the economy, and the benefits of full economic freedom.

The Abaconians have adopted a *laissez-faire* platform and a plan of action aimed at achieving independence. They view the Nassau government as an "uninvited guest" which may be invited to leave at any time. They point out that at least 28 resolutions have been passed by the United Nations affirming a people's right to self-determination regardless of population, geography, or size. Sufficient historical precedent exists to show unequivocally that the Abaconians have a moral and legal right to seek and achieve their goal.

Abaconians have a long history of dedication to freedom. At the height of the pre-Civil War slave trade, they captured slave ships heading for the U.S. and freed the slaves, who became Bahamas settlers. In recent years, before Bahamian independence, the Abaconians attempted to separate themselves from Nassau by petitioning the Queen, to no avail. Today, the idea of independence from the Nassau government has strong grass-roots support.

Abaconians point out that less than one-third of the taxes extracted by Nassau are returned to Abaco in services. The Nassau government's racially-motivated policies deprive many honest, hard-working people of work permits, while a notorious fugitive from justice (who swindled over $200 million) is allowed to stay. Further, the government's policies have discouraged foreign investment,



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and have led to the abandonment of a partially-completed project worth nearly $30 million.

FRIENDS OF ABACO has been organized as a non-profit, charitable organization to assist the people of Abaco. Freinds of Abaco cannot engage in political activities, but will provide educational and material assistance to improve living and working conditions on Abaco. We will help to counteract the effects of interventionism — unemployment, undernourishment, poor education — with direct self-help assistance, training, and educational materials. This assistance should be of benefit not only in terms of immediate economic gains, but also in acquiring additional competence in administrative matters.

We urge all persons concerned with freedom and independence to support Friends of Abaco with a donation. A spark of freedom has been lighted, that could illuminate the entire Caribbean. An enclave such as Abaco, dedicated to the dignity of the individual and to the free market, could be of inestimable value to us all. Noted investment advisor Dr. Harry D. Schultz has stated: "I am sending my donation today; it may be the best investment I ever made, an investment in economic and political freedom." (HSL #313, February 1974)

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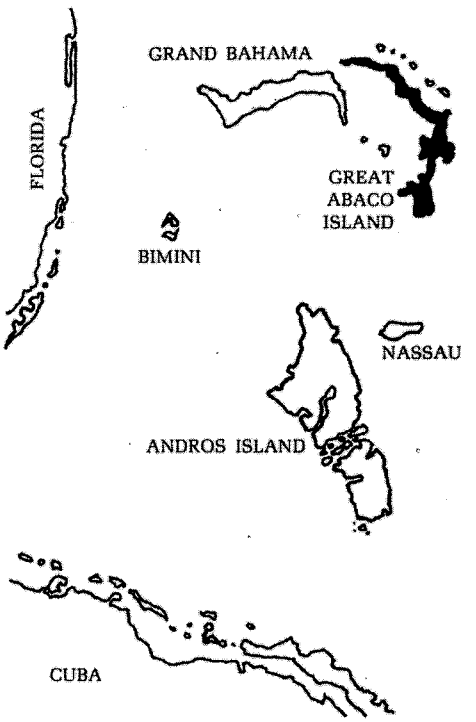
More on Abaco

Abaco is one of the Bahamas Islands, located just to the east of Grand Bahama (home of Freeport). It is 170 miles east of Miami, and comprises 700 square miles in area. Its 6500 people include blacks, mulattos, and whites. Nearly half the population are descendants of American Loyalists who migrated there in 1784-1785. There are 17 small settlements, the largest of which is Marsh Harbour. The economy is devoted mainly to such trades as boat building, fishing, sailing, farming, shopkeeping and tourism. Many Abaconians have migrated to Nassau where they make up a major portion of the city's merchant class. Abaco has the best agricultural land in the Bahamas; its annual rainfall of 60 inches helps provide large crops of tomatoes and cucumbers. The island has two commercial airfields, a major road which runs the length of the island, several excellent harbors, and two deep-water docks. Scheduled airlines arrive on a daily basis and regular shipping runs are made there from Europe and North America.



The Periodic Gathering of the Faithful on Mount Aurum

Robert H. Meier

For a long time the private financial seminar was almost exclusively the province of the European banker and his moneyed clients but now it is coming to America in a big way. Introduced here by men such as Dr. Franz Pick, the concept really seemed to take hold with the advent of Dr. Harry Schultz's highly publicized, notably expensive seminars held in Bermuda and other exotic locations around the world. But what will bring people from thousands of miles away and encourage them to incur the expense of seminar fees and travel to attend what is generally a two-day meeting, listening to groups of speakers (some quite marginal) tell the attendee something that in most cases he already knows? The answer partially lies in the energy and devotion of the " gold bug" to his metal and the warrior-like frame of mind that goes with that commitment. It seems that most of the really successful seminars have orbited around a discussion of *the* metal and in consideration of the investment opportunities it offers: bullion trading and futures, coins, stocks, and all possible permutations therein. The ancillary, but nonetheless important topics generally include foreign currencies, tax avoidance/evasion, overseas banking services, and attacks on the government's meddlesome involvement in personal financial matters—all in all a delightful and worthwhile combination of subjects that bring people back again and again.

This enthusiasm is fully understandable upon the realization that many of these people got their first introduction to the world of gold investments at one of these seminars and were solidly committed to gold when it was still $35 an ounce, so for a time many of them suffered seemingly unending harassment of doubting friends, smug stockholders, and indirectly, an unsympathetic financial press. All that has changed now as their gold investments soar to heights that even the more ardent believers might not have believed possible several years ago. They've had their judgment vindicated by the market and they're enjoying it, and the money, to no end. On one occasion a somewhat detached observer quipped "even a stopped clock is right twice a day" and went on to comment about all the sluggish times gold investments have had. He is partially correct, but then, when you become aware of some of the truly phenomenal gains the "gold bug" has had recently, the sting of past losses (if there were any at all) would probably be insignificant by now. Incidentally, the term "gold bug" is an unfortunate one in that it does not adequately convey the comprehensive financial sophistication that many of these investors have.

The people who attend these seminars are by-and-large a friendly and gregarious lot. Of course, there is an occasional "mystery man." He stays at another hotel, won't give you his name, invariably carries a dirty shopping bag and dresses in early Ellis Island. At lunch you can see him in the lobby, a thermos bottle propped on one knee chewing a ham sandwich he made the night before, while the other attendees are comfortably lunching and trading ideas. No one knows where he came from or where he's going. After hours most of the group will gather at prearranged cocktail receptions and later in the hotel bars (on balance they seem to be moderate or nondrinkers) where they talk to all hours in tight little groups. The men trade anecdotes about their stockbrokers rather than women, and the ladies talk freely of the Carbon Leader Reef and Eurobond yields. Foreign currency parities of years past roll off lips like they were being read directly from a Reuters ticker and business cards with addresses and telex numbers in Zurich, Beirut and Johannesburg shuffle from hand to hand like Cribbage cards. Deals, appointments, and contacts are made until the sun comes up again—commerce at its refreshing best. Many of these people are to a measurable degree de facto Libertarians and in a few cases you'll find some de jure ones as well.

To give the reader a more comprehensive picture of what transpired at the three seminars I attended I have prepared the following detailed listing of events along with some supplementary information.

International Monetary Seminar. Sponsored by Harry D. Schultz. October 12–14, 1973, Montreal, Canada. Approximately 450 in attendance. $600 admission included room and assorted meals and a trip to a gold mine on the 14th.

The list of speakers and their topics follows:

- "Monetary Mud Pie" (View From American Banking) by John Exter, a former vice president of the Federal Reserve Bank of New York. He is also a director of the American South African Investment Company.
- "United Kingdom Economics: Weimarism or Latinism" (A Voice From England) by John Biffen, M.P.
- "Investing in Gold and South African Gold Shares" by David Lloyd Jacob, Joint Resident Gold Expert for Consolidated Gold Fields of South Africa.
- "The International Investor—Problems of Living and Investing Abroad" by Dr. Harry D. Schultz.
- "Australia and the Orient—Is the Mining Boom Over?" by Maxwell Newton, owner-publisher of half a dozen publications on and near the continent of Australia.
- "The Limited German Role in the Monetary System" by D. Franz Josef Strauss, former Defense Minister of Germany and also leader of Bavaria's Christian Social Union Party.
- "Gold: Barbarous Relic or Eternal Backing for War and Commerce?" by Ira U. Cobleigh, feature editor of the *COMMERCIAL & FINANCIAL CHRONICLE* and of the *OVER THE COUNTER CHRONICLE (OTC CHRONICLE).*
- "The Currency Chaos" by Dr. Nicholas L. Deak, founder of the largest foreign money exchange firm in the Western Hemisphere: Deak & Co., Inc.
- "Liberty in an Age of Uncertain Currency" by Dr. Phillip M. Crane, U.S. Congressman from Illinois.

In addition to the regular speakers, workshops were held on silver, Swiss banking, gold coins, currencies and the stock market.

1974 Monetary Symposium. Sponsored by the National Committee to Legalize Gold. January 18–20, New Orleans, Louisiana. Approximately 750 in attendance. $300 fee did not include room.

The list of speakers and their topics follows:

- "Value in General, Monetary Value in Particular" by Dr. John Hospers, Director of the School of Philosophy, University of Southern California and the 1972 Libertarian Party Candidate for President of the United States.
- "The Gold Standard and the Supply of Gold" by Dr. Hans Sennholz, Chairman of the Economics Department at Grove City College in Grove City, Pa., and a leading financial analyst.
- "Humanity, Energy, and Gold" by C. Vern Myers, editor of *MYER'S FINANCE & ENERGY* newsletter.
- "The Monetary Future" by John Kamin, consulting economist and publisher of *THE FORECASTER,* a hard-money investments newsletter.
- "Singing in the Rain" (Will Gold Shares Peak in the Coming Months?) by Thomas J. Holt president of T. J. Holt & Co., publisher of *THE HOLT INVESTMENT ADVISORY* newsletter.
- "The Gold Curve" by Douglas E. Johnston, a gold share expert known for his timely prediction of the 1972 gold move.
- "Gold, the International Money" by Alden R. Wells, author of the *ALDEN R. WELLS MONETARY REPORT,* an investment advisory service, and of the *ALDEN R. WELLS QUARTERLY, a general review of society with an emphasis on* money and taxes.
- "International Monetary Credit Structure" by John Exter.
- "The View from Washington" (prospects for gold legalization, etc.) by Sen. James A. McClure.

Workshops were held on South African gold shares, Canadian gold shares, penny gold stocks, gold and the Dow Theory, Swiss banking, gold and silver coins, currency trading, and tax resistance for profit.

The conference was moderated by John Mc Falls owner of Value-Action Advisory Service of Seattle, Washington.

Dines Gold Seminar. Sponsored by James Dines. February 8–9, 1974, New York City. Approximately 260 in attendance. The $250 fee did not include a room; luncheons and cocktail hours were included.

The list of speakers and their topics follows (several titles have been changed to better reflect the contents of the speeches):

- "The Fallacy of Paper Money and the Renaissance of Gold" by Ira U. Cobleigh.
- "An Examination of Canadian Gold Mines" by Paul Penna, president of Agnico-Eagle Mines.
- "Swiss Banking" by Otto Roethenmund, Senior Vice President of Deak & Co. Inc., and Vice Chairman of the Board of Directors of the Foreign Commerce Bank of Zurich.
- "The Psychology of the Coming Gold Fever" by Richard Russell, editor of the *DOW THEORY LETTER.*
- "A Balanced View of South African Gold Share Investments" by Michael West, editorial director for the *MINING JOURNAL'S QUARTERLY REVIEW OF SOUTH AFRICAN GOLD SHARES.*
- "Gold Share Investments" by John McFalls.
- "Investing in Gold and Silver Coins" by Ben Stack of Stack's Coin Company, New York City.
- "The American Gold Mining Scene" by William Nash, president of Geo Surveys, Inc., Colorado Springs, Colorado.

The sponsor, James Dines, was moderator and periodically addressed the group on issues such as silver investments, inflation and one's personal financial security.

Looking back over all the speeches and opinions I heard the general consensus seemed to be that gold was going higher, and probably much higher (estimates ranged from $200 to $5,000 an ounce by 1976). Opinions on silver as an investment were divided and most commonly cited as a negative factor was the feeling that its value would not hold up in a depression. It was generally agreed that all paper currencies were in for a bad time but that one should still have some cash in a foreign bank account for contingencies. The stock market was viewed as fundamentally weak although it could demonstrate occasional rallies in the near term.

The question now arises as to whether or not you should go to a financial seminar? My answer is yes with some important qualifications. First, be extremely selective in the one you attend. Success breeds imitation and it's no different with financial seminars. Look for speakers with publicly established academic, publishing and consulting service records and you probably will be all right. Second, do your homework before you go. This may make for some duplication during the lectures (they tend towards the basic) but will make your questions much more thoughtful and increase your overall understanding of what's going on. Look for seminars with special workshops held after the speakers have been on the podium. These smaller groups are much more effective in conveying information to the attendees, and perhaps your special investment problems can be discussed. Also most speakers are available at the cocktail hours and luncheons so that you'll have even further opportunities to have your questions answered. Of course the more topics the better if the speakers are quality men. Finally, never forget that the best advice in the world isn't worth a damn unless you act on it.

For further information on upcoming seminars, and to purchase detailed printed transcripts and tape sets of those seminars mentioned here use the following addresses: *Harry Schultz,* 170 Sloane St., London S.W. 1, England; *James Dines & Co., Inc.,* 18 East 41st St., New York, NY 10017; *National Committee to Legalize Gold,* 1524 Hillary, New Orleans, LA 70010. ◻

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On January 18-20, 1974 over 750 people gathered in New Orleans, Louisiana to hear the finest monetary experts ever assembled discuss *Gold, The International Money, Inflation / Hyperinflation / Depression, Long-term Trends in International Financial Markets, Gold Shares, Dow Theory,* and *International Monetary Reform.* The wire services are describing the **1974 Monetary Symposium** as the "Woodstock of the Gold Community."

In commemoration of this historic golden event, the National Committee to Legalize Gold is offering a complete cassette series of all major speeches and workshops. Those pictured in this brochure are featured in the tape series.

We urge you to order today and obtain a recording of the largest monetary symposium on gold ever held!

On February 5, 1974 the National Committee to Legalize Gold initiated a bold legal attack upon the Gold Prohibition laws. One suit has been filed and is now pending in the United States District Court for the District of Colorado. We are now facing the extensive prospect of as many as three appeals to the U.S. Supreme Court within the next three months--possibly even sooner.

To do the job right, and to prosecute a suit that will win, we must be in a position to handle the expenses of a first-class presentation. The Committee asks your immediate financial support for the legal action campaign to **REPEAL GOLD PROHIBITION** in **'74**.

(Further information about the legal action campaign available upon request.)

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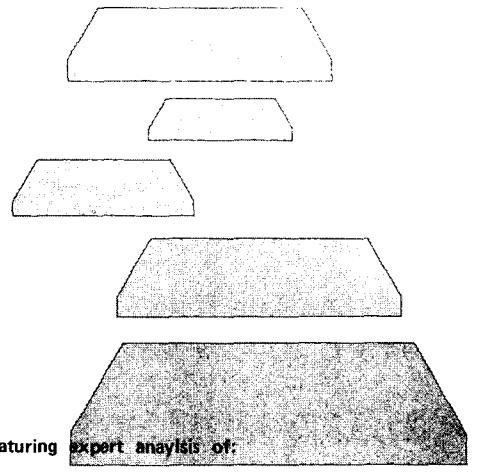

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"Value in General, Monetary Value in Particular."

Why gold and gold redeemable currency are of undeniable value to mankind.

Dr. Hospers is presently the Director of the School of Philosophy, University of Southern California, Los Angeles. In 1972, Dr. Hospers was Libertarian Party Candidate for President of the United States.

DR. HANS SENNHOLZ

"The Gold Standard and the Supply of Gold"

Includes an analysis of the "gold shortage myth".

Dr. Sennholz is Professor of Economics and Chairman of the Economics Department at Grove City College in Grove City, Pa., and is one of the leading financial analysts in America today. He has foretold many months in advance every recession since WWII. In more than 250 publications he has discussed all aspects of the American financial and economic dilemma.

ALDEN R. WELLS

"Gold, the International Money."

Perceptive insights into the forthcoming gold exchanges in international money markets.

As owner of Alden Rice Wells, Inc., publishers, he has authored for nine years the *Alden R. Wells Monetary Report* — an investment advisory service—and for seven years the *Alden R. Wells Quarterly* — a general review of society with emphasis on money and taxes.

C. VERN MYERS

"Humanity, Energy, and Gold".

Is humanity faced with unavoidable world wide depression? Why the energy crisis is far more serious than anyone believes. What will happen to paper currencies and the price of gold.

Mr. Myers is editor of *Myer's Finance & Energy*...a high-powered newsletter featuring gold investments to energy crisis information.

JOHN KAMIN

"The Monetary Future".

Future inflation that will stagger the imagination. Some surprise predictions for '74 . . .Gold?. . . the Stock Market?

John Kamin is consulting economist and publisher of *The Forecaster*--a forward-looking newsletter that monitors the future of hard money investments.

TOM HOLT

"Singing in the Rain".

Is it possible that gold and gold shares may peak in the coming months? How will deflation affect the stock market and hard money investments?

A self-made man, Thomas J. Holt is the President of New York-based T. J. Holt & Co. which publishes *The Holt Investment Advisory* and manages investment portfolios for private investors.

DOUGLAS E. JOHNSTON

"The Gold Curve".

How high gold in '74? What will be the reaction of gold shares to an explosive bullion market?

Vice-President, First of Texas, Inc., and gold share expert known for his timely prediction of the explosive 1972 gold move. For four years he has contributed articles to the *Alden R. Wells Quarterly*.

JOHN McFALLS

Master of Ceremonies for the 1974 Monetary Symposium

John McFalls is the owner of Value-Action Advisory Service in Seattle, Washington; a life member of the Committee for Monetary Research and Education; and a co-founder of the National Committee to Legalize Gold.

JOHN EXTER

"International Monetary Credit Structure".

Is the world's money system on a crash course to world wide economic disaster? Mr. Exter's timely viewpoints on gold, international money reform, and the danger of the current credit pyramid.

Mr. Exter became senior vice-president of First City National Bank in 1959. At Citibank he was international monetary advisor for the bank's International Banking Group with special responsibilities for relations with foreign central banks and governments. In 1972 he took early retirement to become a private consultant.

Sen. JAMES A. McCLURE

"The View from Washington".

His latest views on the prospects for gold legalization in '74, how the energy crisis relates to gold; will the Arabs demand gold or gold-backed currency? The prospects for international monetary reform.

RICHARD RUSSELL

"Gold and Dow Theory".

A fast moving workshop of questions and answers on a wide range of subjects including: gold, silver, the stock market, Dow Theory analysis, the explosive potential of U.S. and Canadian "penny golds," and much more!

Richard Russell is publisher of *Dow Theory Letters*--timely and informative analyses of international market trends and gold developments.

This historic Cassette Series will also feature speeches by William Tehan of P. R. Herzig & Co., Inc., entitled "Outlook for South African Mining Investments", and George T. Steve, Managing Editor of Pick's World Currency Report and Pick's Currency Yearbook, entitled "International Inflation and Gold".

Mr. Tehan discusses the possibility of a stock market crash of unprecedented proportions and what will happen to gold shares in the coming months. Question and answer sessions are included in the recordings as well as a special workshop on South African gold shares.

foreign correspondent

PROGRESS IN DENMARK

Taastrup, Denmark. In the beginning of December 1973 we had a general election here in Denmark which could almost be termed a "parliamentary revolution." The four old parties that have been leading Danish politics through all of our parliamentary history were reduced from having the support of almost three-fourths of the electorate at the former election in 1971 to little more than 50 percent at this election (the percentage of votes cast was 88.7). By far the larger part of the straying votes went to various nonsocialist parties with the major share to the tax-negating Progress Party led by Mogens Glistrup (which was discussed in my column in the October 1973 *REASON).* The result is that the precarious balance which has existed for a long time between the Socialist and the Conservative-Liberal parties has been thrown off and a completely new political situation has emerged.

The results of this election may be roughly summarized as follows:

1. The Social Democratic Party (moderate socialistic), which has been the largest party since 1924, has maintained this position; but out of 175 seats in parliament it now has only 46 as compared to 70 before the election. Its supporting party, the Socialist Populistic Party (nonmoderate socialistic), lost 6 seats and now has a mere 11.

2. The three old Conservative-Liberal parties, which had the remaining 88 seats, now have 58 taken together. (The reason why they were not able to control a majority in parliament is that, in addition to the 175 seats, 4 more seats are reserved for representatives from Greenland and the Faroe Islands—enough of these have supported the socialist parties and hence can be said to have determined the political course in opposition to the majority of the inhabitants of Denmark proper. It sure does not pay to be an imperialistic power!)

3. The remaining 60 seats have been gained by parties that were not represented before the election (20 to socialistic parties and the rest to nonsocialistic parties) and among these the Progress Party is by far the most important with 28 seats, which makes it the second largest party. This alone is something that has never happened before in Danish politics: that a new party—and even one with a goal that is completely in opposition to the existing trend—has gained support from one out of every seven possible voters!

The main conclusion to be drawn from the result of the recent election is that a lot of Danes seem to be more than normally disillusioned with the established welfare state and that they have therefore voted for those parties that promise reduction of the administration (and the welfare programs ?) and thereby reduction of the heavy tax burden.

After such a reorganization of the parliament and with the seats distributed to 10 parties (as compared to 5 before the election), the formation of a new government was necessarily a difficult matter. After two weeks of negotiations, the Liberal Left (which is not socialistic but the one of the three old Conservative-Liberal parties which traditionally represents the farming population) with only 22 seats undertook the task and is now busy with proposals concerning the energy crisis and the ever wilder rolling inflation. At this time it is impossible to predict whether they will be able to carry out the wishes of the voters as expressed in the election or whether we will have a new election very soon. But it is at least evident that they will have to cooperate effectively with a wide range of other parties, so there is hope that the present parliament will be a better expression of the opinion of the majority of the population than the former one was.

The reaction of the press to the result of the election (which incidentally coincided very well with the opinion polls taken during all of 1973) was, in general, as could be expected: shock, indignation, and accusations of immorality, egoism, and the wish to destroy the welfare state against those antisocial individuals who had *dared* to vote for something different than the established trend—particularly those who had voted for the Progress Party. The public however does not seem to be so discontented with the outcome: at least the opinion polls taken after the election do not show any great deviations.

The public opinion in the immediate future will, however, depend on how the new parties conduct themselves in the debate in the months to come. This is especially true for the Progress Party which still does not have a comprehensive political-philosophical programme and which is exclusively known by the controversial public appearance of its founder and leader, Mr. Glistrup. Most of the members of his group in parliament are quite unknown to the public.

As a personal comment, I do not think that this "parliamentary revolution" should be regarded too optimistically. It's true that it is a clear manifestation of a real dissatisfaction with the high taxes and to some extent with the meddling of the welfare state into the affairs of everybody; it's a real relief (at least to some of us) that the socialist trend has been subdued. But it's also true that it's a revolution without the necessary ideological basis and popular understanding of the principles involved, and it is therefore primarily negative in its content. The Danes that voted for the Progress Party are not Libertarians and I'm quite convinced that if that party had had a real Libertarian platform it would not have been represented in parliament today, but would have been repudiated as totally immoral! There is simply no real understanding and very little knowledge of such principles today in Denmark and it's highly dubitable that the Progress Party has the strength or the intention to pave the way for it.

I'm sorry if I'm disappointing you—I would be very happy if I'm proven wrong and shall report about the development in due time.

Anne Brincker

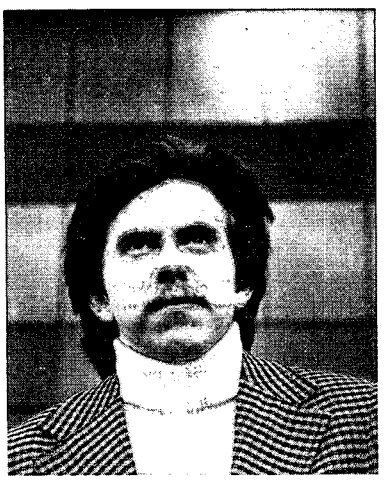
ANTHEM FOR DOOMED YOUTH

What passing bells for these who die as cattle?
Only the monstrous anger of the guns
Only the stuttering rifles' rapid rattle
Can patter out their hasty orisons.
No mockeries for them; no prayers nor bells,
Nor any voice of mourning save the choirs,—
The shrill, demented choirs of wailing shells;
And bugles calling for them from sad shires.
What candles may be held to speed them all?
Not in the hands of boys, but in their eyes
Shall shine the holy glimmers of goodbyes.
The pallor of girls' brows shall be their pall;
Their flowers the tenderness of patient minds
And each slowdusk a drawing-down of blinds.

Wilfred Owens

John James would like to represent you in Congress.

No matter where you live.



John James thinks it's time for libertarians to have someone who will represent their ideas in Congress.

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Which means that come next January, you're going to have to rely on the Representative from your own District to speak for you.

Unless you do something to improve your chances.

That's where John James can help. If you'll help him get elected to Congress from Denver, he'll make sure you've got someone to turn to.

Someone who will fight uncompromisingly for individual freedom.

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Someone you can count on to throw a monkey-wrench in the gears of the engine of destruction.

Someone who will introduce bills to repeal regulations, rather than add more.

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And if everyone who reads this ad will contribute just one percent of the amount he paid in Federal taxes last year, we'll have it.

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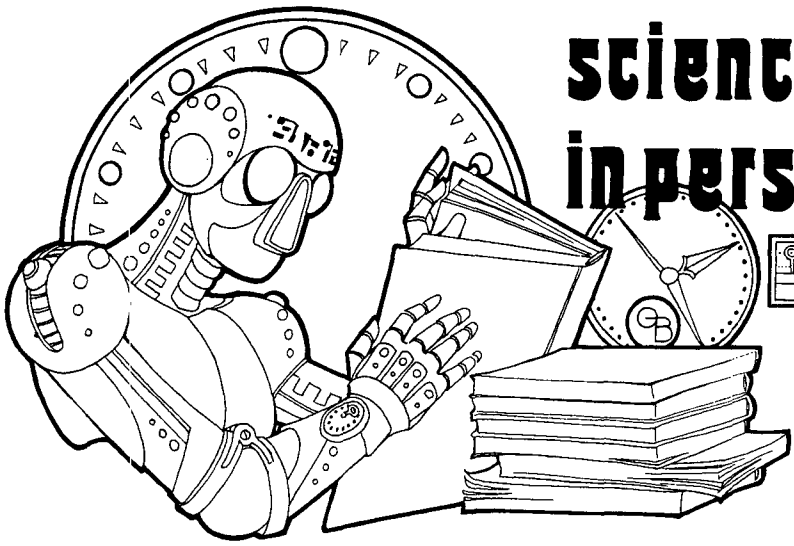

science fiction in perspective

JOHN J PIERCE

John Pierce's Science Fiction column alternates monthly in REASON *with Davis Keeler's Money column.*

BEHIND THE CURTAIN

The expulsion of Aleksandr Solzhenitsyn from the Soviet Union was only the latest episode—although perhaps the most dramatic so far—in the new repression of Soviet literature that has been gaining momentum for the last six years.

Soviet science fiction, which enjoyed a remarkable renascence in the decade following the late Nikita Kruschev's de-Stalinization campaign, has shared the reaction against "liberalism" in recent years. But, remarkably, the effect of the repressive movement has, until recently at least, been far less severe than on "mainstream" literature.

Science fiction has traditionally been the most "liberated"—in a relative sense, of course, bearing in mind the nature of the Soviet system—literature in the Soviet Union. This may account for its wide popularity with Soviet youth—book editions of 150,000 or more often sell out overnight, and total sales in the millions are not uncommon for some works.

Even before the Soviet Revolution, there had been a tradition—albeit a minor one—of SF in Russia. Besides the imitators of Jules Verne, most of whose works are forgotten, there were utopian SF writers, Marxist and otherwise. Best-known of these was Aleksandr Bogdanov, whose *RED STAR* (1908) and *ENGINEER MENNI* (1913), used Mars as a setting for Marxist utopias in much the manner the German Kurd Lasswitz had earlier used that planet to portray a Kantian utopia.

Bogdanov is a revered figure among Soviet SF critics, even though *ENGINEER MENNI* is considered to have "deviationist" ideas on evolution—rather than revolution—as the key to progress. After the Revolution, Bogdanov strove to be more Papist than the Marxist pope, founding a literary "Proletcult" that was so extreme in its views that even Lenin later disowned it.

Although the Revolution is credited with having inspired a rebirth of SF in the Soviet Union, this rebirth actually took place during the time of the New Economic Policy from about 1923 on, when restrictions were few and private publishing was allowed for a time. Even the Marxist utopias and "Red Detective" thrillers emphasized in official critical histories date from this period.

More than 200 SF works were published in the 1920's, and many were quite inventive. Graal Arelsky, a futurist poet, anticipated America's Raymond Z. Gallun in his moody treatment of interplanetary contacts in such works as "Gift of the Selenites" (1926) and "The Man Who Visited Mars" (1927), while N. I. Mukhanov independently invented space opera—complete with death rays and interplanetary spaceship battles—in *FLAMING ABYSSES* (1924).

Ivan Vinnichenko's *THE SOLAR MACHINE* (1924), a semi-Marxist utopian work, was remarkable for speculating on the possible impact of technology to abolish scarcity and make abundance a social problem—a theme that didn't become popular in American SF until the 1950's. "Red Detective" thrillers exploited such scientific frontiers as laser-like rays (Aleksei Tolstoy's *GARIN'S DEATH RAY,* (1926) and nuclear chain reactions (Vladimir Orlovsky's "Revolt of the Atoms," 1927) in much the manner American pulp SF thrillers did—though from an opposite ideological viewpoint.

BELYAEV

Aleksandr Belyaev (1884-1942) was the most prolific, and creative, of the early Soviet SF writers. His best-known novel, *THE AMPHIBIAN* (1928), is a sympathetic account of a youth who has been surgically adapted to live underwater by a sort of benevolent Dr. Moreau. In conveying the emotions of a man to whom an entire new world has been opened—yet who is cut off from normal human relationships—Belyaev was far ahead of his time. *THE AMPHIBIAN* has an adventurous plot—the hero, Ichthyander, is a kind of undersea Tarzan—and humanistic philosophy that gives it a lasting appeal.

Purists were suspicious of science fiction in general for its "cosmopolitan" attitudes—foreign locales and an apolitical humanism were common in works by writers like Arelsky and Belyaev. Even the utopias were too romantic—V. D. Nikolsky's "In a Thousand Years" turned on a love-triangle, with a time-traveller from our era vying with a man of the future for the affections of the heroine in a world of cities suspended from transcontinental skyways, singing plants and atomic energy (which Nikolsky, startlingly, predicted would be unleashed in 1945).

In 1929, the Russian Association of Proletarian Writers (RAPP) launched a campaign against science fiction, and within a few years had virtually driven it out of existence.

Belyaev managed to keep working—as late as 1935, he could write of space travel in *A LEAP INTO NOTHINGNESS,* although the astronautical works which had been common in the 1920's (such as S. L. Grave's 1926 "A Journey to the Moon") had generally come to be frowned on. But for the most part, freedom of imagination was eliminated from what science fiction was allowed during the Stalin years.

Typical SF of the 1930's was devoted to down-to-Earth themes like the development of Siberia, as in Grigory Grebnev's *ARCTANIA* (1937), or to glorifying Soviet military power in its struggle with the Capitalist world, as in Grigory Adamov's *THE SECRET OF TWO OCEANS* (1939). When Yuri Dolgushin wrote *THE GENERATOR OF MIRACLES*—a highly imaginative work dealing with concepts like thought-transmission and immortality—in 1939, he couldn't find a book publisher for it (and didn't, until 1959). For the most part, SF plots were limited to melodramas about foreign spies trying to sabotage the Five-Year Plan.

World War II brought an end to the hard-line Stalinist SF, paving the way for an orthodox—but low-key—school of writers who emphasized scientific enterprise more than ideology. "Practical" science was stressed—in Vladimir Nemtsov's "Shadow Under the Earth" (1948), a device to see through the Earth is used to make fabulous discoveries of mineral deposits; in Georgy Gurevich's "The Soaring Poplar" (1951) fast-growing trees are invented to reclaim deserts. Gigantic sheep revolutionize animal husbandry in Abram Paley's *TAUSEN'S ISLAND* (1948), and a shoe leather that won't wear out is the subject of Viktor Saparin's "The Magic Shoes" (1955).

RISE OF UNORTHODOXY

Ivan Yefremov (1907-72), who wrote similarly conservative SF in the late 1940's and early 1950's, was the first to take advantage of de-Stalinization in 1957, with *ANDROMEDA*—a cosmic utopian novel set thousands of years in the future which, although it seems tame (both imaginatively and ideologically) to us, was revolutionary to the Soviets.

ANDROMEDA was the focus of a Great Debate between the "Warm Stream" critics who wanted change in SF and the "Cold Stream" critics who didn't—and the former carried the day.

Although Yefremov was the immediate beneficiary, his imaginative vision was relatively conservative—in "The Heart of the Serpent" (1959), for example, he replies to Murray Leinster's "First Contact" by arguing that contacts between different intelligent species must always be friendly because they will all be good Communists. And his "aliens" are 100 percent humanoid, even though they breathe fluorine!

But Yefremov's victory over the "Cold Stream" critics opened up science fiction to dozens of new writers with fresh and often unorthodox viewpoints.

Most prominent are the brothers Arkady (b. 1925) and Boris (b. 1933) Strugatsky. Their most popular novel, *HARD TO BE A GOD* (1964) centers on a team of experts sent to "guide" the evolution of an extraterrestrial society—and the tragedy of the hero who comes to realize his superiors really don't know what is happening there, but can't get them to change their thinking before disaster strikes. Although hardly anti-Communist, the novel is a telling critique of ideological orthodoxy.

In "Wanderers and Travellers" (1963), the Strugatsky brothers counter the anthropomorphic blindness of writers like Yefremov towards intelligence in nonhumanoid forms, while in *FAR RAINBOW* (1964), a disastrous experiment gone wrong on a planet used as a scientific laboratory dramatizes their message against the dehumanization and overspecialization of science.

MONDAY BEGINS ON SATURDAY (1965) is a satire on the bureaucratic misuse of science, while *THE SECOND MARTIAN INVASION* (1967) attacks the sort of conformism and complacency that allows the "invasion" to take place virtually unopposed (the title is an ironic reference to H. G. Wells' "first" Martian invasion). And in *THE TALE OF THE TROIKA* (1968), a committee of bureaucrats originally created to check the plumbing system manages to take over a whole country in a brilliant satire of how Power Corrupts.

A sort of humanism that an earlier age would have condemned as "bourgeois sentimentality" marks many Soviet SF works of the 1960's. Individual heroism on the frontiers of space and science is emphasized in stories like Vitaly Krapivin's "Meeting My Brother" (1962) and Valentina Zhuravleva's "Storm" (1961). In Yevgeny Voiskunsky and Isai Lukodianov's "A Farewell on the Shore" (1964), a scientist who has contrived a means for the body to age all at once, instead of gradually, is faced with the certain knowledge of when and how he will die—and must learn to face this with courage and dignity.

Fadim Shefner's "A Modest Genius" (1968) is remarkable for taking the part of a solitary inventor who, for his own amusement, devises things like water skates so he can skim across the lake with his true love—while a mediocre scientist is showered with official honors for worthless inventions like a can opener that weighs five tons and costs 400,000 rubles. Vladimir Grigoriev's "The Horn of Plenty" (1964) similarly sympathizes with an eccentric genius against the bureaucrats.

Ilya Varshavsky built up quite a following with his satires on the foibles of science and society like "The Molecular Cafe" (1963) and "Preliminary Research" (1965), which are almost as free-wheeling as American social-satirical SF.

The relative freedom on the 1960's was also shown in works like Voiskunsky and Lukodianov's "Formula for the Impossible" (1964) in which astronauts come across an alien race that has degenerated by allowing a master computer to take over planning of its economy and society. Gennady Gor, in "The Minotaur" (1967) and other works dealt with problems of communication with alien systems of thought.

Soviet authorities sharply curtailed publication of science fiction after the invasion of Czechoslovakia in 1968, but even after this some authors—particularly the Strugatsky brothers—were able to bring out some works loaded with social criticism, such as *THE INHABITED ISLAND* (1969). They got in trouble when *THE UGLY SWANS*, a thinly-veiled attack on anti-Semitism, was published abroad last year, but are still writing SF with toned-down satirical overtones for home consumption.

More typical now, apparently, are conservatively ideological critiques of Capitalistic militarism, as in Sever Gansovski's "The Proving Ground" (1969). Orthodox social criticism had already been represented in the works of Anatoly Dnieprov—some incredibly simple-minded, like "The World in Which I Disappeared" (1961), in which a mad scientist sets up an experimental model that proves the Marxist exploitation theory; others modestly-imaginative for all their limitations, like "The S*T*A*P*L*E Farm" (1964), in which cloning is used to turn out standardized humans.

But the more liberated Soviet SF has been read by hundreds of thousands, and is undoubtedly still wielding its intellectual influence. This gives an element of hope to an otherwise dismal cultural outlook.

Note: I am indebted to the researches of Darko Suvin, John W. Andrews and Robert Magidoff for some of the information used in this column.

book review

THE BILLION DOLLAR SURE THING. By Paul E. Erdman. New York: Scribners. 1973. 248 pp. $6.95.

Reviewed by J. M. COBB

When it comes to a question of money, there are two types of people to be found within libertarian circles—the wheeler-dealer-entrepreneur-investor, and the gold-coins-buried-in-the-backyard-saver. The former likes libertarian ideas because of the promise of freedom of action, and the latter subscribes because of the promise of solid economic value, secure from taxation and depreciation of net worth.

Both types ought to read this novel.

The action of the book revolves around the attempt by the United States government to fix the price of gold at a high level and thereby make the greenback dollar more in demand. Of course, the news leaks out about two weeks in advance of the date this financial maneuver is scheduled and the scene shifts to the Swiss banking community, the Russian foreign trade bank, and the adventures of cops and robbers attempting to cover up the fact that there was a leak, and find the source.

This novel seems to have a strong pro-capitalist bias, which sneaks through once in a while—usually very subtly. The libertarian reader will find himself cheering at the events inside Russia, since it reinforces our opinions of the party bureaucrats (who almost make a couple of billion and cause great harm to the dollar at the same time, but who get tripped up by internal politics and *lose* a billion instead).

The dynamics of the Swiss banking houses are portrayed in detail, with special digressions by the author to explain to the reader exactly what is happening in non-technical terms. For this information alone, the book is worth checking out of a local library. For the whole plot, however, the book is worth ordering from one of our noble libertarian book services.

The author, Paul Erdman, ought to know enough about this sort of operation, inasmuch as he was president of the United California Bank in Basel, Switzerland, until it landed him in jail. His bank had been speculating in cocoa futures, and lost; and then his staff decided to doctor the books to hide the loss. During the 10 months which Erdman spent in jail, he wrote this novel. Naturally, one of the characters ends up in jail—so we benefit from a real-life description of Switzerland such as a tourist would never learn.

The wheeler-dealer-entrepreneur-investors among us will find themselves fascinated by the developments in the gold market as the word spreads about the coming devaluation. The mechanics of how these markets work is true in the story, only the names have been changed to protect the men behind the scenes. Interestingly, only one man in the market really knows the secret U.S. Treasury plan—all the others figure it out by shrewd guessing and the observation of market movements.

The gold-coins-buried-in-the-backyard-savers among us should appreciate the portrayal of the banking community as a gang of subtle swindlers using other people's money to pile it up for themselves. The best part of the whole book, in this reviewer's opinion, is when the little guy who *really* figured it all out by himself gets shafted by the police and has his fortune stolen by the banker, who simply "cancels" all transactions of the previous day (in which a fortune had been made). An episode like that pushes my cynic button—you *know* that's how things *really* turn out all the time anyhow.

From the standpoint of an economist, the events in the book are all correct and logical. There is none of the hokum which occasionally crops up in science fiction and other speculative fiction, to assume some contradiction of the laws of human action. This reviewer found himself hoping all along that the dollar would crumble, as all of the government-characters in the book feared. Alas, the Russians goof it up. Yet the story should be instructive to people who naively believe that (1) government-managed money is a safe and secure system; or (2) that having a fixed price for gold in terms of dollars (and so-called redeemable dollars) is the way to prevent the problems caused by government-management. Obviously my own pet scheme of the Anti-Inflation Constitutional Amendment is the answer, but enough axe-grinding.

Probably because he was writing the novel during a jail term, Paul Erdman lets justice triumph in the end. If you enjoyed *NONE DARE CALL IT CONSPIRACY,* you will love the ending of *THE BILLION DOLLAR SURE THING.* ◻

J. M. Cobb is the author of "What You Should Know About Monetary and Fiscal Policy" which appears elsewhere in this issue.

YOU CAN PROFIT FROM A MONETARY CRISIS. By Harry Browne. New York: Macmillan Publishing Co., Inc. 1974. 397 pp. $8.95.

Reviewed by E. RAYMOND PASTOR

In 1970 Harry Browne published *HOW TO PROFIT FROM THE COMING DEVALUATION.* It became a national best-seller. Harry became an internationally known investment counselor and his views on the significance of monetary developments are in great demand.

Anyone who had acted on Harry's investment recommendations since 1970-71 has seen his gold mining stocks triple, his silver bullion double, and his Swiss francs appreciate as much as 60 percent vis-a-vis the dollar.

Last year Macmillan published Harry's second book, *HOW I FOUND FREEDOM IN AN UNFREE WORLD.* It is a noneconomic treatise of a wholly personalist libertarian philosophy, whose theme is pursuing your own freedom and happiness without having to change the world or the people around you.

Now Harry has come out with the long awaited sequel to *DEVALUATION;* it was released by Macmillan in February. *YOU CAN PROFIT FROM A MONETARY CRISIS* comes to grips with the whole range of market dynamics, rather than focusing just on the monetary situation as in the first book.

Few people really understand the magnitude of the present world economic situation and what it will lead to. Each individual should have an understanding of the basic economic problems that afflict the U.S., as well as a grasp of the underlying forces that are bringing the world to a

general monetary collapse.

The current economic and political events that are unfolding are not isolated incidences, nor are they inexplicable. They are part of an inevitable pattern of consequences brought about by previous causes that can be easily identified.

The first part of the book is a succinct explanation of the principles of cause and effect of economic laws. And it is one of Harry's basic premises that with an understanding of objective economic laws, the appropriate investments for the rational individual become self-evident.

Given a rapidly depreciating currency, hyperinflation, a devastating five year bear market, wage and price controls, continual balance of trade deficits, and an accrued balance of payments deficit of over $100 billion, it would be prudent to not have dollar-related investments.

These investments include: common stocks, bonds, mutual funds, and real estate, not to mention the more obvious losers like savings bonds, social security, and savings accounts. Even diamonds, art, and numismatic coins can be vulnerable, if one's investment objectives are safety and preservation of assets in light of all possibilities.

Given a fiat currency monetary system since 1968 and no convertibility since 1971, it would be prudent to exchange dollars for currencies with gold backing *and* convertibility. Here Harry is extremely helpful in providing a comparative analysis of foreign currencies in terms of gold backing reserves and their relative value to the dollar and to all other currencies.

Given the very likely possibility of runaway inflation and the social and economic chaos *that* would bring (along with the probability of martial law and dictatorial government), it would be prudent to have your assets out of the country and a retreat out in the hinterland. In fact, for optimum safety, Harry suggests having *everything* in Switzerland, except your retreat!

As for investments in the "barbaric relic," Harry prefers South African gold mining stocks (kaffirs) to U.S. or Canadian. As for gold coins, he prefers those with the lowest numismatic premiums. And as for gold bullion, nice work if you can get it! Harry believes the potential for gold is $200 by year end and at least $500 by 1978.

Harry also foresees an explosive price situation some time in the next few years that will drive the price of silver through the roof. He sees the potential in the next two to five years for $10 silver as very probable because of the monumental imbalance in supply and demand for the white metal.

In addition, Harry discusses the merits of some speculative types of investments that are suitable for the bolder investor in these times of monetary crises, such as margin accounts, commodity futures trading, currency futures, and short selling common stocks. The book also contains sections on sample investment programs, where and how to get information, recommended reading, charts, and a glossary.

In sum, *YOU CAN PROFIT FROM A MONETARY CRISIS* will give the reader a grasp of the nature of the monetary mess and what he can expect to happen in the foreseeable future. It is, therefore, prudent reading for any individual who would like to preserve his (or her) personal autonomy in the coming years—where nothing less than investments for survival will do. ◻

Ray Pastor is a Commodity Account Executive with Hayden Stone Inc., White Plains, New York. He has a finance degree from the University of Miami, an M.A. from the University of Maryland, and was formerly associated with the Pacific Coast Coin Exchange New York Office.

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movies

REVIEWED BY
CHARLES BARR

• In refreshing contrast to much of today's knee-jerk propaganda, **CONRACK** is a "message" film that can be enjoyed on its own terms. Idealistic without being preachy, optimistic without being naive, the movie vividly illustrates the value and potential of the human mind, even under circumstances of appalling neglect. Jon Voight stars as a white teacher at a rudimentary all-black elementary school on a poverty-ridden island off the coast of South Carolina. The movie, based upon a true incident, details the teacher's attempts to overcome the island children's appalling ignorance. (Most of them don't even know the name of their country.) His unorthodox and highly imaginative teaching methods succeed in igniting sparks of interest and enthusiasm among the jaded children, but clash with the value system of the school's black principal (Madge Sinclair), who has inherited a legacy of despair which she is dutifully attempting to pass on to the next generation. Voight also runs afoul of the superintendent, a "benevolent racist" played by Hume Cronyn with a dignity that the part does not deserve. Paul Winfield has an interesting role as the island's bootlegger, who trades whisky for reading and writing lessons. But the heart of the movie is found in the interaction between Jon Voight and the children. He cajoles, teases and taunts them, catching them up in his unrestrained enthusiasm as he mixes classical music and swimming with more basic subjects. The students think he's crazy, but respond in spite of themselves, learning for the first time to enjoy their own minds. Martin Ritt, who directed *SOUNDER,* has another winner in *CONRACK,* and hopefully the movie will be a liberating influence on the situation it has so skillfully brought to light. Rated "PG."

• There's no denying that **BLAZING SADDLES** is funny. In assembling this parody Western, Mel Brooks and his cohorts pile joke upon joke, with reckless abandon and no regard for race, creed, continuity or good taste. The movie is not internally consistent enough to be a satire, or clever enough to be sophisticated; essentially, it is a 95-minute collage of low-comedy sketch material, with the whole adding up to less than the sum of its parts. But it is chock full of jokes. Cleavon Little stars as a black sheriff imposed upon an unwilling Western town, with Harvey Korman and Slim Pickens as the villains attempting to destroy the town for their own profit. Gene Wilder is Little's amiable sidekick, while Madeline Kahn does a bawdy tandem imitation of Marlene Dietrich and Mae West. For this reviewer, the type of comedy featured in *BLAZING SADDLES* is best taken in small doses; a full-length feature is overdoing it. Rated "R."

• For a movie about someone with all the answers, **MAN ON A SWING** provides few answers of its own. Joel Grey stars as a mysterious stranger who telephones a police station, offering his alleged powers of clairvoyance to help solve the brutal murder of a young woman. Cliff Robertson is the police chief, obsessed with the murder and willing to accept help even from such an unlikely source. The movie starts out promisingly enough, liberally sprinkling clues about the murder and about Joel Grey's seeming authenticity as a mentalist. Then the doubts begin to creep in. But rather than aiding the exposition, they serve only to muddy the waters, making the case as difficult to unravel as Watergate. Screenwriter David Goodman attempts to balance the evidence for and against Grey's clairvoyant powers as evenly as possible, without drawing any definitive conclusion. As a result, even the eventual solving of the murder is dramatically unfulfilling; the movie seemed to promise more. Frank Perry's uneven direction infects the performances: Joel Grey's psychic re-enactment of the crime from the victim's point of view eventually grows tiresome, while Cliff Robertson underplays his role from start to finish. Dorothy Tristan has a thankless part as Robertson's wife. The sound track deserves some special award for irritation; incidental noises drown out whole sentences, forcing the viewer to concentrate on the words and diverting his attention from the film as a whole. But maybe it's just as well. Rated "PG." ◻

Jon Voight (right) whips up enthusiasm in his class in scene from CONRACK.

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REASON celebrates its sixth birthday this month by publishing the largest issue in our history, and we have plans to bring you many more outstanding articles and features in the coming months. Scheduled for future issues are exclusive interviews with such individuals as Milton Friedman, Edith Efron, *PENTHOUSE* publisher Bob Guccione, and libertarian psychiatrists Thomas Szasz and Peter Breggin.

REASON's June issue will feature a timely analysis by economist D. T. Armentano of the "monopoly" problem in the petroleum business, plus investment counselor Ed Crane's valuable article, "All You Ever Wanted To Know About Bonds (and More)," and other features.

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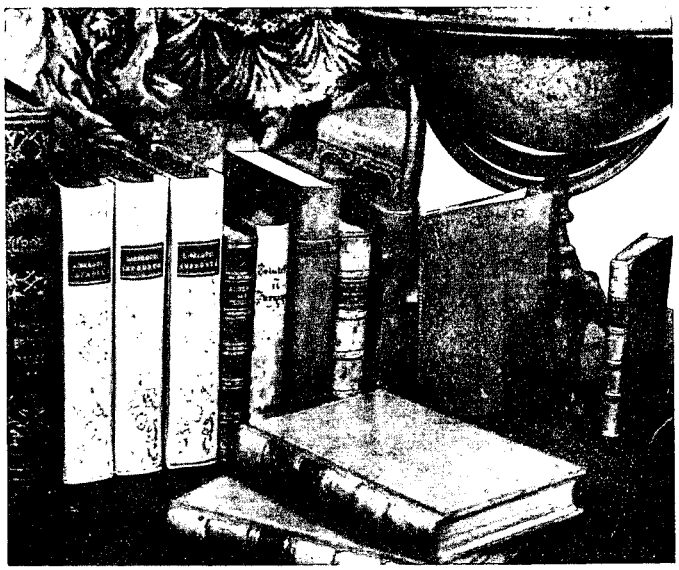

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viewpoint

DAVID BRUDNOY

THE INDIVIDUAL, THE GOVERNMENT, AND YAF

Young Americans for Freedom, the major conservative youth organization, recently sponsored, through its Young America's Foundation, a weekend conference in Philadelphia on "Privacy: the rights of the individual, and the role of government." W. C. Fields, when asked for his epitaph, replied: "On the whole, I'd rather be in Philadelphia." I don't know if it's really that bad in the City of Brotherly Love, but I had no time to find out since I had to leave Philadelphia bright and early the morning following the conference for New York City en route to Boston.

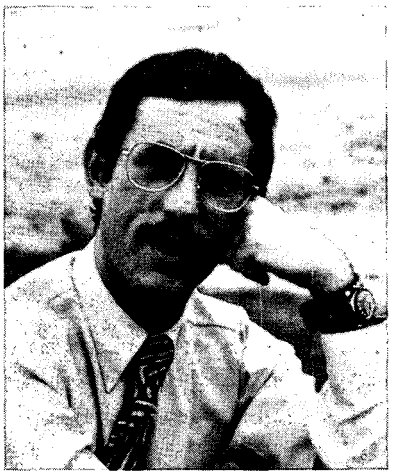
In its more libertarian moments, YAF stands strongly against government supervision of the citizenry's lives, although when it comes to victimless crimes—well, another story, anon. On the second morning of the conference, Mr. Tom Charles Huston, formerly a White House aide to President Nixon, and peripherally involved in planning some of *those* events about which we hear so much, spoke on government surveillance of private citizens. Although he tried to convince his listeners that at the height of the disturbances, back a few years, those in the know thought they knew enough to justify some of those taps on phones and the like, the thrust of his speech was opposed to such government surveillance.

Later in the day, the former editor of the YAF publication, Jerry Norton, spoke eloquently in favor of the volunteer military, pointing out that the draft military is most certainly a government invasion of privacy. His colleague on that panel, Ronald Docksai, national chairman of YAF, delivered a splendid address on various forms of population "control" and experimentation, including cloning and other forms of asexual reproduction. Docksai voiced his concern, shared, I believe, by most of his listeners, that in our fascination with science we may be rushing into a situation of almost sci-fi tinkering with the individual. It made one think.

I spoke after lunch on victimless crimes, urging an end to government censorship of any form of reading matter, any form of consensual sexual activity among adults, and the like. I was rebutted by Prof. William A. Stanmeyer of Georgetown University Law School. Mr. Stanmeyer takes the traditionalist line, and sees no difference between the libertarian-conservative position I espoused and the libertinism I derided. The emphasis in his talk was on Virtue, which, he avers, the government has a right to enforce.

Mr. Stanmeyer, we learned, was so incensed by a piece I had written some months ago in *NEW GUARD* along the lines of my talk at the conference, that he set out to challenge it and is now sitting on a 300-plus-page manuscript outlining his views. I await the book eagerly, though to be frank, I know it already. One has heard it again and again, although no doubt Stanmeyer's approach will be scholarly and inventive.

At bottom, the traditionalist approach is one seeing the worst possible consequences of extended freedoms in the personal sphere. And so: what, he asks, will happen—what will happen to our social fabric if people can do what they want, read what they want, sleep with whom they want where they want? Why, natch, we'll all go straight to the dogs. Ah indeed, we might well go straight to the dogs, but I am inclined to think that route will be traveled because of other disturbances in our society than those I would like to see decriminalized. The Stanmeyer view, one shared certainly by many tens of millions of Americans, is not easily dismissed just because it is authoritarian and morose.



No other issue so raised the interest level at the YAF conference as that which Mr. Stanmeyer and I debated. Maybe sex and related matters are the conservative cuckoo, as someone—Gore Vidal?—once said. I'm not sure. I do know that you will find these economically libertarian people all across the conservative spectrum, but the minute the very idea of decriminalizing crimes without victims rears its head, the conservative "movement" falls into pieces, one side, mine, taking a strict libertarian line, the other retreating to the collectivist fold: let us have government *enforce* morality, by all means, by any means, some say. Mr. Stanmeyer's forthcoming book should make its case well, as he did in debate with me in Philadelphia. I fear that his view is destined to prevail for sometime yet, perhaps for many decades more. It is repugnant to the libertarian mind, but then, the American is no more a libertarian than he is a vegetarian, perhaps less the former than the latter. ◻

Dr. Brudnoy's viewpoint appears in this column every third month, alternating with the viewpoints of Murray Rothbard and Tibor Machan.

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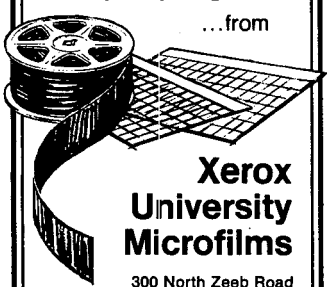

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reason profile

Special Issue Editor Robert Meier can be described as a man of many interests. After attending college for several years he enlisted in the Army, serving from 1966 through 1969. He saw duty in Vietnam near the Cambodian border, and later, as an escort sergeant in the Army Funeral Service.

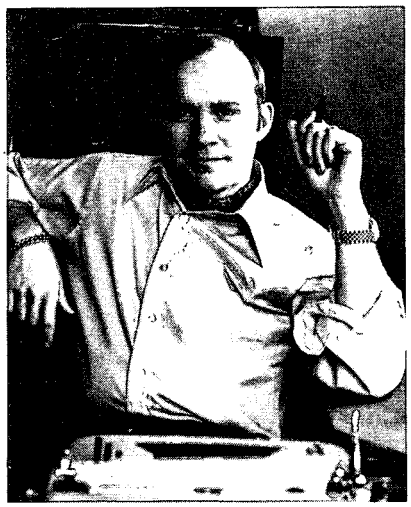
After the military, Meier attended the Gemological Institute of America and then worked for a time as an apprentice appraiser/salesman for the prestigious jewelry firm of Arbogast & Associates. He studied finance at Northern Illinois University and last year was the first recipient of a newly created Money and Banking Award.

Having a long standing commitment to the free market, he was formally introduced to the libertarian movement by the activist Paul Varnell. Meier is now serving as Fund Raising Chairman, as well as being on the Executive Committee, for the National Libertarian Party. "I've been excited about the party since its inception. On a per-capita basis, I'm convinced that it is one of the finest collections of multi-faceted talent ever assembled for a political purpose. Now all that really remains is for the bulk of them to quit massaging each other's ideology and get down to work."

Meier enjoys a diverse set of part-time activities. A balletomane of long standing, he has a ballet studio in his basement and has studied classical dance off and on for 10 years. "The Captain even got used to seeing my ballet slippers and tights at Saturday inspection!" He has very specific tastes in music with some of his current favorites being Satie, Scriabine, and Faure. He enjoys fine dining and important wines and collects fine art. An avid shooter, he especially enjoys handgunning.

Meier is not regularly employed and spends his time managing a diverse set of special projects and working closely with his banker father on various business matters, "We evidently missed the generation gap that was the rage several years past." Meier also lectures and moderates at financial seminars.

A voluminous reader, he is obsessed with finding timely and definitive sources of financial information. On a regular basis



he particularly enjoys reading Robert Bleiberg of *BARRON's*. Some of his recreational reading favorites include Ian Fleming (The James Bond Series), Forsythe *(THE DAY OF THE JACKAL),* and Huysmans *(AGAINST NATURE).*

At 28, Meier is a supremely happy man and takes a child-like delight in his sybaritic pursuits. One expects his future will never be dull.

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trends

This column reports trends in the advancement of individual liberty and the rediscovery of economic freedom. Readers are invited to submit material of potential interest.

NEW TAXPAYER VICTORIES

The intrusion of the federal government into our lives is nowhere more ubiquitous than on our paychecks, where the withholding of Social Security and income taxes takes an increasingly large bite each year. Until recently the wage-earning taxpayer was helpless to resist federal withholding, but two recent decisions offer new hope. In two unrelated cases, taxpayers have successfully fought back against Social Security and income taxes, respectively.

The income tax case was decided by Judge Clarence Newcomer of the U.S. District Court in Philadelphia. The case involved two employees of the American Friends Service Committee who, for religious reasons, oppose paying taxes for the support of war. In December 1969 they requested their employer to stop withholding 51.6 percent of the tax for which they were liable, and AFSC agreed to the request. The employees filed regular tax returns on the remaining 48.4 percent, and contributed an equivalent 51.6 percent to a nondefense, "humanitarian" government agency. These checks were subsequently returned and the employees bank accounts attached for the unpaid tax.

In May 1970 the two employees and AFSC filed suit against the IRS, attacking the withholding method of collecting income taxes from employees who have religious scruples against supporting war. On December 31, 1973, Judge Newcomer ruled the withholding tax requirement of the Internal Revenue Code "unconstitutional as applied to the facts of this case in that it operates as an abridgement to the free exercise of the religion of [the] plaintiffs . . . ." The decision forbids the IRS from withholding 51.6 percent of the plaintiffs' federal income tax, but permits it to continue to collect this portion of their tax via attachment of their bank accounts, the following year. Since the case was not filed as a class action, the judge could not extend the ruling to cover other taxpayers in similar circumstances. But he noted that AFSC "may seek to exempt future employees by first seeking such exemption from the Internal Revenue Service and finally the court, if necessary."

Just such an exemption was recently sought—and obtained—with regard to Social Security taxes, but in this instance the tax itself was challenged. James Dale Davidson, executive director of the National Taxpayers Union, formally waived his Social Security benefits and has refused to pay his Social Security taxes on grounds of nonreligious conscientious objection. Davidson's case rested on a recent Supreme Court ruling that conscientious objection to the draft must not exclude those whose positions derive from a consistent moral philosophy. Although he had hoped the IRS would take him to court in a test case, the IRS decided to settle with Davidson privately. They have—and Davidson is now exempt from Social Security taxes. The National Taxpayers Union is now seeking funds and volunteers to force the IRS into court on the issue, in order to establish the point for all potential conscientious objectors. Although Davidson himself is self-employed, there appears to be no reason why similar conscientious objection would not be applicable to Social Security *withholding,* as well.

SOURCES:

- "Court Limits Power to Withhold Taxes," Marjorie Hyer, *WASHINGTON POST,* January 21, 1974.
- "Anti-Social Security," Shirley Scheibla, *BARRON'S,* January 21, 1974.

AFTERMATH: THE OBSCENITY RULING

In its 1973 ruling re-establishing a legal basis for the censorship of "obscenity," the Supreme Court chose to ignore the evidence accumulated in Denmark regarding the alleged harmfulness of pornography. Since the Danish government decontrolled written works in 1967 and visual material in 1969, the Institute of Criminal Science has continued keeping careful records of sex-related crime patterns. Between 1959 and 1970, the Institute found, there was no discernable change in the rate of occurrence of rape in Copenhagen. Other sex offenses, however, have decreased sharply: exhibitionism is down 58 percent, peeping is down 80 percent, molesting of female children is down 69 percent. These figures appear to show that the presence or absence of pornography has no effect on the frequency of rape, and may act as a (victimless) substitute for other forms of sex crimes—a safety valve, in effect. Thus, since pornography does not incite crime, the Supreme Court's decision is simply the imposition of a particular code of morality by force of law.

Fortunately, the people involved in writing, filming, distributing, selling, and exhibiting works which might be judged "obscene" are not taking the new censorship lying down. (And neither are the consumers: *The Devil in Miss Jones* was the fifth largest-grossing film of 1973 in *VARIETY's* annual survey, while *Deep Throat* ranked 11th; the two grossed $7.3 million and $4.6 million, respectively.) The major groups involved, and their activities, are as follows:

- *Publishers* are divided, with many reacting in fear while others refuse to be ruffled. Kenneth McCormick, chairman of the Freedom to Read Committee of the Association of American Publishers reports that a certain amount of "self censorship" is going on among publishers, and notes that the level of prosecutions has been less than expected. Among the publishers taking a firm stand against changing policy because of the Supreme Court ruling are Pocket Books (Simon & Schuster), Viking, and Random House. The latter provided immediate legal defense for a bookseller in Orem, Utah, who was served with a summons in November for selling *A CLOCKWORK ORANGE,* considered taboo under a municipal ordinance banning "lewdness and obscenity." The charges were subsequently dropped.

- *Librarians*—the American Library Association's Freedom to Read Foundation has joined with the Association of American Publishers in petitioning the Supreme Court to rehear its five 1973 obscenity cases, and is inviting other appropriate groups to join it in this endeavor. Vice president Everett T. Moore points out the danger to libraries and literature inherent in the Supreme Court's extremely subjective "community standards" criterion for obscenity. Moore also points out that although the Court has not reversed its earlier ruling permitting the private *possession* of pornography, it has potentially forbidden all means of *obtaining* such material.

- *Film producers*—Samuel Z. Arkoff, board chairman and president of American International Pictures, takes the position that "legitimate" films are endangered more than porno films by the Supreme Court rulings. Due to the "community standards" provision, "porno films made on a shoestring will survive

because they are so cheaply produced that they can earn back their cost in a few big cities. . . . But the serious pictures made on the scale of *Carnal Knowledge* cannot recoup their costs by playing in a handful of cities or illicit movie speakeasies. . . . These serious, controversial, costly pictures will simply not be produced, or if produced will be so compromised that they will be pap . . ." Arkoff thereby challenges the position of Jack Valenti of the Motion Picture Association of America, who wants to sacrifice the porno films to the censors for the sake of saving the "legitimate" studio films. Arkoff, by contrast, calls for a broad-based alliance of all film producers, distributors, exhibitors, the press, and various civic organizations to safeguard freedom of expression.

• *Film distributors* are also concerned, none more so than the Adult Film Association of America, who held their sixth annual convention in San Diego in February. The Supreme Court recently accepted an *amicus curiae* brief prepared by the Association's legal counsel, Stanley Fleischman, in the Court's pending *Carnal Knowledge* case. Fleischman is working with the Association to plan further legal strategy in all the states where members operate. There are now some 80 obscenity cases pending in the Supreme Court, more than in any other field, at a time when crime is at record levels and court calendars are jammed with cases involving real crime. Still, progress of a sort is represented by recent surveys showing that a majority of big-city residents (65 percent in Kansas City, 75 percent in Los Angeles) agree that an adult should have the right to see any pictures of sex acts in movies or magazines.

Perhaps the most telling commentary of all on the censorship issue is the appointment of Marty Snyder to the nine-member movie censorship board in Clarkstown, New York. Mr. Snyder, who claims to be "no stuffed shirt," has been blind for several years.

SOURCES:

• "Pornography in Denmark," *PLAYBOY,* January 1974, p. 53.
• "Two of Top 50 Films from the Porn Belt," Vernon Scott, UPI (Hollywood), January 24, 1974.
• "Publishing Houses Policing Selves Due to Court Ruling," Eric Pace, New York Times News Service, January 20, 1974.
• "Librarians Speak Out: Court's Obscenity Rulings Aren't Going Unchallenged," Everett T. Moore, *LOS ANGELES TIMES,* September 3, 1974.
• "Porno Ruling Held Peril to Big Films," *LOS ANGELES TIMES,* September 21, 1974.
• "Adult Film Group in Quest to Gain Respect," Arthur Knight, *LOS ANGELES TIMES,* February 17, 1974.
• "Marty Can See What Others Might Miss," AP (New City, NY), September 21, 1973.

SAYING NO TO CONTROLS

Although most American oil companies have meekly complied with the federal energy czar's decrees, two large companies have taken principled stands against them —and have backed up their words with legal actions. First to take action was Gulf Oil, which has filed suit against the government's crude oil allocation scheme. Despite the fact that Gulf's management has been able to secure enough crude to operate their refineries at 91 percent of capacity, the Federal Energy Office has ruled that all crude beyond that needed to operate at 76 percent capacity be sold to those companies with less than enough to run at 76 percent. Gulf has rightly challenged this Robin Hood system as confiscatory. In announcing the company's suit, Gulf executive vice president Z. D. Bonner stated, "Without a doubt this amounts to the unwarranted and, we feel, unlawful taking of private property."

A second challenge to FEO controls occurred two weeks later, when Union Oil Company filed suit against FEO demands that it sell fuel to independent oil dealers in preference to its own dealers. Union is defying the order, and has filed suit in U.S. District Court in San Francisco asking for a preliminary injunction against the FEO order. Union states that the allocation orders are invalid and unconstitutional because they deprive dealers of their property without due process of law. Union and two of its dealers filed the suit as a class action on behalf of all 740 Union dealers in Los Angeles and Orange Counties. A Union representative pointed out that the company could have made the same amount of money selling the gasoline to independent stations, but felt an obligation to its own dealers.

The practical effects of the government's petroleum controls are by now so obvious that even such publications as *TIME* are pointing out that many European nations have abandoned controls and allowed prices to rise, with the result that long lines at gasoline stations have disappeared. And *TIME* quotes FEO officials as privately conceding that the crude oil allocation program has been an "unmitigated disaster." As of this writing energy czar Simon has asked Congress to "suspend" the program for 90 days—hopefully, a face-saving way of phasing it out altogether.

SOURCES:

• "Gulf Will Challenge Order to Sell Its Oil to Other Refiners," Robert A. Rosenblatt, *LOS ANGELES TIMES,* February 12, 1974.
• "Union Oil Challenges U.S. Order to Supply Gasoline to Independents," *Ibid.,* February 27, 1974.
• "Facing the Shortage Alone," *TIME,* March 4, 1974.

THE GOLD AND SILVER BOOM

The long lines these days are not just in front of gas stations. In many cities equally long lines have been forming outside of coin shops, as anxious persons from all walks of life seek to convert their depreciating paper money into gold and silver coins. Luis Vigdor, coin manager of New York's Tordilla & Brookes, stated, "We can't even handle the volume any more . . . I've never seen a situation like this." He reported lines of customers waiting one to two hours to get a chance to buy gold. One New York coin dealer has taken to staying in a hotel, to escape the constantly ringing telephone at home and at work. Coin sales at Pacific Coast Coin Exchange have quadrupled in the past year, while gold coin sales increased threefold in the past *month* at Deak & Co. in Los Angeles.

In Santa Barbara, one Rexall drug store is advertising all items as 50 percent off if purchased with U.S. silver coinage, hardly a good deal at current silver prices, but very possibly a harbinger of things to come. Another Santa Barbara store, Lanello Reserves, is selling survival kits consisting of low-moisture food supplies, along with reverse osmosis water purifiers, silver ingots, and 22-karat placer gold. Vice president Murray Steinman notes that "No economic system unbacked by gold or silver has survived more than 40 years without economic catastrophe."

In New York, mutual funds are turning to gold mining stocks in a big way. Win-Cap, a former go-go fund, has been renamed Research Capital and turned into a gold fund. President Charles B. Johnson believes that "Gold is going to be the primary monetary asset eventually, and its free market value isn't reflected in gold shares yet." John C. van Eck's International Investors Inc. got into gold in 1968 and is now the country's leading gold fund. Its assets have increased from $68 million last December to $125 million in March.

Government spokesmen can denounce gold as a "barbarous relic" all they please, but people all over the world are turning to gold (and silver) as protection against government debasement of the currency. Before long the politicians will have to face the facts and return to a monetary system based on real value.

SOURCES:

• "Americans Buying Gold Frantically," AP (New York), February 28, 1974.
• "New Gold Fever Undercuts Value of Paper Money," Ronald L. Soble, *LOS ANGELES TIMES,* March 2, 1974.
• "Survival Kits Offered in Crisis," Chet Holcombe, *SANTA BARBARA NEWS-PRESS,* February 20, 1974.
• "Shifting into Gold," *BUSINESS WEEK,* December 8, 1973. ◻

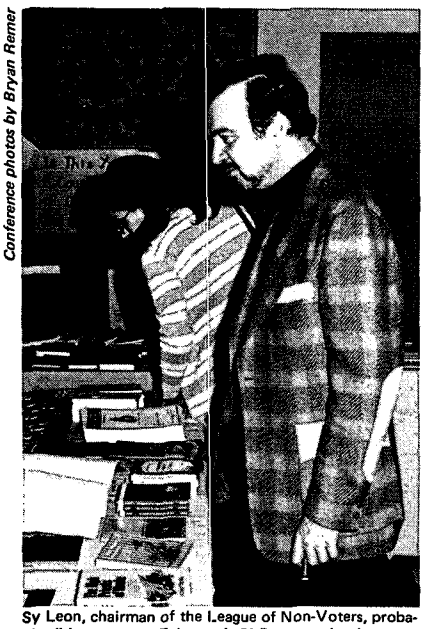
frontlines

CALIFORNIA LP CONVENTION '74— *Frontlines* correspondent **Bryan Remer** reports:
While Harry Browne was over in San Francisco pushing his latest book, over 100 members and guests of the **Libertarian Party of California** helped fill the Claremont Hotel in Berkeley and worked their way through an exhausting four-day convention, beginning February 15.

Former Vice Presidential candidate **Tonie Nathan** opened the convention officially the next morning with "The Caveman Concept," a survey and refutation of the idea that violence is necessary to achieve social change but that reason is not. Past Presidential candidate **John Hospers** delivered the keynote address, "The Concept of Values" and their application to current political/cultural reality, which included a chilling perspective on non-voluntary commitment to state mental institutions.

Other libertarian celebrities attending the convention included: **Roger Lea MacBride** from Virginia, who cast his electoral vote for the Hospers-Nathan ticket in 1972; **Dr. Antony Sutton**, of Stanford's Hoover Institute; **Karl Bray**, tax resistance leader from Utah; **Mike Oliver** from Nevada, leader of the "new countries" projects; **Sy Leon**, president of **Rampart College** and chairman of the **League of Non-Voters; Poul Anderson**, noted science fiction author; **Hank Hohenstein** of the "San Diego Ten"-IRS trial; and also visitors from the Alaska, Washington and Oregon Libertarian parties.

Conference photos by Bryan Remer



Sy Leon, chairman of the League of Non-Voters, probably did not vote at February's CLP convention in Berkeley.

Saturday's business dealt mostly with amendments to the state party constitution and bylaws, which was less dreary than expected. The most significant modification, one which would have a telling effect at the last of the convention, was the voting procedure for national, state and party office candidates, which provided an automatic alternative choice called "none of the above."

With Sunday came the hoped-for success that was embarrassingly absent at Fresno in 1973—a state party platform. This year the platform committee had generated 13 prospective planks, and with additions from the floor, 15 planks were voted approved, usually by wide majorities. Some significant planks dealt with "victimless crimes," the energy crisis, transportation, welfare, and taxation.

As in Fresno last year, the delegates voted to retain the national LP's statement of principles for California's platform. And again, the statement survived a weak attempt by several members to extract the phrase containing "laissez-faire capitalism." Ironically, it was a member of the visiting delegation of the **Peace and Freedom Party** who delivered an ovation-getting rebuttal to the proposal. The measure was defeated almost unanimously.

(The Peace and Freedom Party is undergoing its own schism into two distinct camps—social democrats and anarcho-capitalists. Representatives of the more libertarian-oriented group attended the convention to gain information and to introduce their own candidates for public office.)

Monday, the floor was cleared for the main event—the election of party officers and the nomination of statewide candidates. Because of the constitutional amendment mentioned previously, each office seeker now found himself running against a potentially preferable candidate —"none of the above." **Ed Clark** retained the state chairmanship, and the race for governor became this new provision's test track.

Hoping to get some writing done during his Fall '74 sabbatical from USC, Dr. Hospers had openly disqualified himself from candidacy in party nominations. But he had stated privately that in the event of a deadlock or lack of clear mandate for an announced candidate, he would consider a draft nomination.

Gubernatorial front-runner **Hal Jindrich**, systems analyst and psychological consultant from Mountain View, waged a vigorous but failing campaign against "none of the above." When Dr. Hospers then accepted a late nomination, a second ballot gave him the clear majority. **Bill Susel** of Los Angeles, Hospers' campaign manager in 1972, won the nomination for Lt. Governor. (Hal Jindrich received the party's endorsement of his bid for State Superintendent of Public Education.)

Bill Susel and John Hospers, the LPC's candidates for California's Lt. Governor and Governor.

The deadlock-vote twist, almost a surprise, settled the last of the weekend's two major questions—the platform and the governor. The 1974 convention was over. The "nonpolitical party" had grown a little stronger.

NITTY-GRITTY
Suppose you're a libertarian interested in running for public office or you're part of an activist group interested in getting media attention—where can you go for advice about what to do? How do you set up a car wash and how much money can you expect to net? How do you get your candidate on a radio show? Both the **Society for Individual Liberty** and the **Libertarian Party** have published good action manuals telling *what* to do. It has remained, however, for the participants in New Yorker **Sandy Cohen's** campaign for the U.S. House of Representatives to tell us tyros *how* to do the nitty-gritty work any activists have to cope with.

The vehicle for this enlightenment is called—not surprisingly—*NITTY-GRITTY*, and is a monthly six-page mimeographed newsletter, formerly edited by **Ralph Blanchette** and now by **Serena Stockwell.** Back issues have contained data on running a carwash, hustling $2000 worth of raffle tickets, setting up a press conference, contacting community groups, etc., as well as interesting, practical-oriented interviews with Cohen's campaign manager, **Ellen Davis**, and **Gary Greenberg**, Free Libertarian Party candidate for New York City D.A. in last November's elections. With the election only eight months

away *NITTY-GRITTY* is no longer accepting subscriptions, but back and future issues are available for 50¢ each.

And if you're involved in any sort of public education project (such as a political campaign, letter writing, or giving editorial replies on TV or radio) you would be well advised to invest $5 in a set of Sandy Cohen's campaign statements. A lucid and prolific writer, Cohen has been producing a blizzard of press releases on everything from inflation and the energy crisis to the government's ban on blacking out TV coverage of pro-football games—and they've been getting published, which is what it's all about.

Some Cohen For Congress volunteers: *Front row: (left to right)* Ellen Davis—Campaign Manager (nag), Sanford Cohen—"Star", Jennifer Cohen (on lap)—official stamper, Carole Cohen, Brock Cohen (on lap), *Second row:* Olga Harney, Cheryl Blanchette, Ralph Blanchette, Serena Stockwell—Editor of *NITTY-GRITTY*, *Third row:* Joyce Starpoli, Vivien Wadlin, Norman Betros Jr., Lisa Corrado, Lynn McCormick, Linda Lawhun.

To order a set of press releases, buy *NITTY-GRITTY* back issues (there are about 10 so far), or contribute to Sandy Cohen's energetically waged campaign please contact **Citizens for Cohen,** P.O. Box 1776, Poughkeepsie, NY 12601.

UC EXTENSION OFFERS COURSE

The University of California, San Diego Extension is offering a course entitled *Liberty, Property and Contemporary Social Problems,* which is of interest to all those who oppose the ever increasing control by government of all aspects of an individual's life. Among the speakers are **Dr. John Hospers,** professor of philosophy at USC, on "Libertarianism: Philosophy and Program"; **Bernard Siegan,** La Jolla attorney, on "Property Rights and the Environmentalist Movement"; **M. Stanton Evans,** editor of the *INDIANAPOLIS STAR NEWS,* on "The Media in Free Society"; **Judith Thornton,** economics professor at the University of Washington, on "Liberty and Property in the Soviet Union"; and **Sara Baase,** San Diego chairman of Libertarian Alternative, on "The Women's Movement: A Libertarian View." Readings for the course will include material by Hayek, Hospers, Friedman and Rothbard.

The lectures will be on Tuesdays at 7:00 p.m. from April 2 to June 4 on the UCSD campus. Interested persons may contact the UC Extension, (714) 453-2000 ext. 2061, and ask for information about Economics X419.

NOTES:

John Hospers will be speaking at Kean College on April 22 at 1:30 p.m. Call Department of Philosophy, Kean College, Union, NJ for full details . . . Libertarian **Liz Jacobson** has announced her candidacy for the U.S. House of Representatives from the Sixth Congressional District (San Francisco and Marin Counties). The special election to fill this seat will be held in June and volunteers, contributions, etc. are urgently needed. To help out or to get more information contact **Richard Winger,** 3201 Baker Street, San Francisco CA 94123 . . . Free Libertarian Party member **Guy Riggs** has announced his candidacy for New York State Assemblyman from the 99th District. For further information contact Riggs at 32 Saddle Rock Drive, Poughkeepsie, NY, phone (914) 462-0613. Between Riggs running for the Assembly and **Sandy Cohen,** also of Poughkeepsie, running for Congress, any Dutchess County citizen who hasn't heard of libertarianism has got to be more out of it than former area resident Rip Van Winkle . ◻

A MODERN STUDY IN MORAL PHILOSOPHY FROM THE *INSTITUTE FOR HUMANE STUDIES*

THE FOUNDATIONS OF MORALITY
(398 pp.), by Henry Hazlitt

Hardcover – IHS price: $8.50
(retail, $12.00)
Softcover – IHS price: $2.25
(retail, $ 3.50)

Morality, Henry Hazlitt maintains, is essential to the survival and functioning of human society, and the basis of morality is social cooperation. While cooperation serves the interests of the whole of society, it is also the great means by which the individual is able to best serve his own interests. Within this framework the long-run interests of the individual and those of society coincide.

As an economist, Hazlitt shows that modern economics provides answers to the problems of human interaction. He draws an illuminating parallel between economic values and moral values, showing in what sense morality and moral values are "subjective" and in what sense they are "objective". The intimate connection between ethics and the rule of law is also demonstrated.

Hazlitt clarifies such issues as equality and inequality, free will and determinism, egoism and altruism, rights, and morality and religion. He skillfully contrasts the ethics of capitalism and the ethics of socialism and argues that the former promote freedom and justice and embody the cooperative ideals which lie at the heart of the good society.

This book, which is in the great line of utilitarian thinking that comes down from Hume, Adam Smith, and Bentham, is lucid, persuasive, and soundly argued.

John Chamberlain

Henry Hazlitt makes an all-out, one-man assault on the central citadel of ethical theory, where the most formidable problems are concentrated.

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publisher's notes

• **ARTICLES WANTED:** The editors of *REASON* are seeking knowledgeable persons to produce articles on the following subjects:
(1) *Copyrights vs. copying machines:* What kind of intellectual property rights are involved in the widespread use of office copiers to duplicate articles and sections of books, and how should they be protected? This subject cries out for some clear thinking. A good source of background information is "Copyright, Public Policy, and Information Technology," by Nicholas L. Henry, *SCIENCE*, February 1, 1974, p. 384. The wider issue of paying residuals to authors whose books are loaned out by libraries might also be addressed in this context.
(2) *Gun control laws:* It is becoming increasingly difficult for an American to exercise the right to "keep and bear arms." *REASON* would like to publish an article describing the extent of freedom still remaining, pointing out states with the fewest or least onerous restrictions, ways of exploiting loopholes in the gun laws, actual enforcement policies, etc., and how to prepare—*now*—for the likelihood of even greater restrictions in the future.
(3) *Alternatives to public schooling:* What alternatives are open to parents who want to keep their children out of the decaying public school system? How does one find a worthwhile "free school"? Of particular interest, how can parents educate their children at home without running afoul of the law? Both case histories and general principles would be welcome.

Persons knowledgeable in any of the above areas should write for information before submitting manuscripts. Write Reason Author Information, Box 6151, Santa Barbara, CA 93111.

• **STUDENT ACTIVISM:** While American students are livening up the news with "streaking" on campus, students in several African countries have recently engaged in serious disorders, including strikes and demonstrations. In the west African country of Niger, students went on strike, demanding payment of an increased allowance, three meals a day and transport to and from school. The crisis was solved and students returned to their classes after the government conceded on all three points, according to the *CHRISTIAN SCIENCE MONITOR* (March 7).

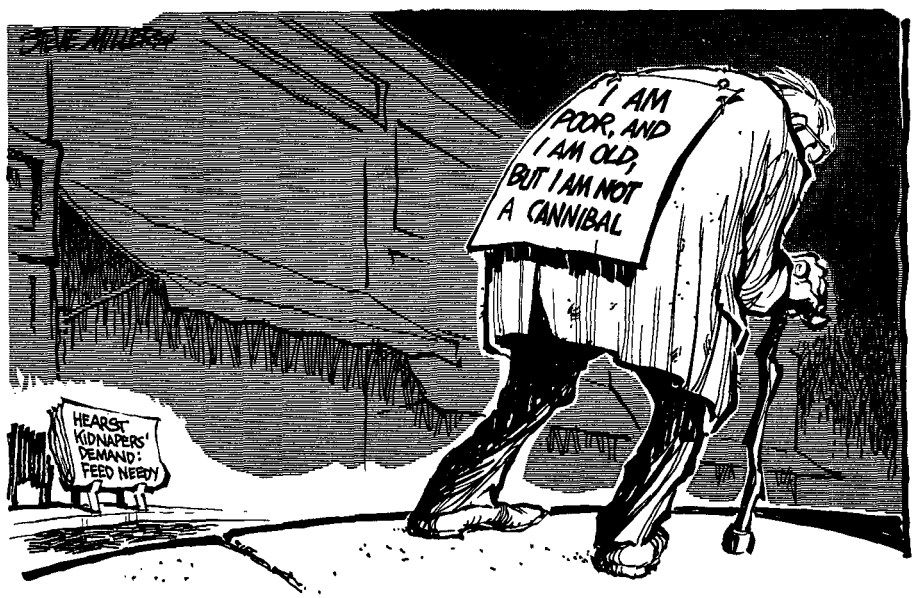
• **COMPULSORY CLOTHING:** Although the new "streaking" fad has been criticized by some as sinful and immoral, we haven't yet seen many American politicians propose that students be put in jail for nonviolent public nudity. However, in Belgium, the Labor Ministry has recently ordered *all* people to wear specified clothing for their job, beginning January 1. As reported in a dispatch from Agence France-Presse (Feb. 26), Belgium's Labor Minister said that clothing suitable for their work will be "compulsory for all trades and professions whether they are cooks, surgeons, firemen, sewermen or welders." The Labor Minister said the clothing requirements would include standards for safety, hygiene and esthetic design, and "would give a boost to the textile industry."

Meanwhile, in the United States, in a discussion of the propriety of streaking, one observer wrote in the *LOS ANGELES TIMES* (March 15), "If God wanted us to run around in the nude, he would have made us that way."

• **NEW RULES FOR PRESS AND POLITICS:** In a fascinating column, "No More Mr. Nice Guy," in *NEW YORK MAGAZINE* (March 11), Richard Reeves writes that there is a harsh "new tone" creeping into the middle of American political journalism. Observes Reeves, "The country, it seems, has had it with its politicians, with the inoperative imbeciles in the White House and the equivocating eunuchs in Congress. And if familiarity breeds contempt, you can imagine how the press feels." Reeves, who recently described Nelson Rockefeller, Ronald Reagan and John Connolly as "hypocritical bastards" after watching them campaign for President at the Southern Republican Conference said he had felt good afterwards to receive letters and calls from other political reporters "saying essentially: about time!"

Although Reeves could hardly be accused of advocating laissez faire, he did state "The people are right. Politicians *are* a bunch of no-good lying hypocrites," and concedes that "A lot of influential people in press and politics consider [Teddy] Kennedy an overage adolescent and are more than a little frightened about what kind of President he would be." Reeves says the politician he would "most not want to be" is Kennedy, and predicts that reporters "are going to write some very unpleasant things about Teddy." He expects the new approach to political reporting to show up in the networks, the *NEW YORK TIMES* and other publications not noted for their irreverence. Encouraging news, Mr. Reeves!

• **NEW STYLE POLITICAL TRAINING:** A retired madam, Sally Stanford, who ran San Francisco's best known brothel during the '30s and '40s holds a seat on the City Council in Sausalito, California. Although she now operates a fashionable restaurant on Sausalito's waterfront (just north of San Francisco), we can't resist the observation that, considering what our politicians have been doing to us, Ms. Stanford has had useful training for her elected position.



WILL PEOPLE REALLY LISTEN TO LIBERTARIAN IDEAS?

DR. JOHN HOSPERS BELIEVES THEY WILL! WHY? BECAUSE an ever-growing number of conscientious American citizens keep writing and calling him saying, "I like what I hear . . . " "Tell me more . . . " "How can I help?" Because when he appears on the campaign trail, on TV, on radio and when he has articles published, the response is usually positive and enthusiastic in favor of this new political philosophy.

In June of 1972, Dr. John Hospers consented to become the first presidential candidate of the Libertarian Party. With no thought of being elected, but only that he would be able to inform individuals about the new Libertarian ideas, he campaigned extensively across the country. He is a nationally respected professor and former chairman in the department of philosophy at the University of Southern California. At the time of the '72 elections, he had just written the first full-length book on the new political philosophy,

LIBERTARIANISM: A Political Philosophy Whose Time Has Come.

AT A TIME WHEN NO OTHER LEADING LIBERTARIAN SPOKESMAN CAME OUT IN SUPPORT OF THE FLEDGELING LIBERTARIAN PARTY, DR. JOHN HOSPERS, WITHOUT ANY POLITICAL AMBITIONS SAID, "YES . . . I WILL BE YOUR SPOKESMAN IF YOU DESIRE IT."

A Fulbright scholar, Dr. Hospers has for years been a noted and distinguished author, having written numerous works on political philosophy. Several of his textbooks are used in colleges and universities throughout the world. When he made the decision to step forward in '72, it was not taken lightly.

What was the outcome? Without a doubt—people listened! The politically virgin Libertarian Party ticket achieved an unprecedented historical, if technical, 3rd place finish with thousands of balloted votes. However, an electoral vote is what put the Libertarians on the political scoreboard. With the power of this vote, libertarianism became a national political fact—and a respected political philosophy.

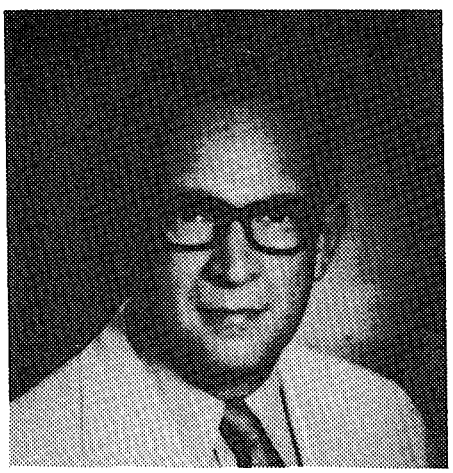
1974! Today, the Libertarian Party of California is getting geared up for the November elections by fielding a slate of candidates for local and state offices who are prepared to present libertarian ideas clearly and enthusiastically to the voters. Dr. John Hospers, has once again consented to lead our slate as our gubernatorial candidate; drafted in Oakland during the February California convention.

So again he will be travelling; this time throughout the state, speaking to all elements of the political spectrum. Again he will be appearing in all media—actively campaigning for laissez faire. Hundreds of California Libertarians will be working on the campaign . . . but we must try to give them the support they need in order to reach the minds of other Californians.

That's why we are asking for your moral and financial support now. Let us know you are with us and watching us. It is far better than having "big brother" watching us without your help! We have the people, the incentive and the program. We need the means in order to be heard. Our track record is spotless and shows that we'll put your contribution to excellent and proper use. $5 means 300 copies of a leaflet. $10 means 100 brochures. $100 finances mailing to 800 voters. $1,000 will establish a campaign headquarters stocked with literature and volunteer personnel.

Help us; help yourself; and help give the people some new ideas to listen to.

DON'T WAIT: THE TIME FOR LIBERTARIANISM HAS COME!



Dr. John Hospers
Candidate for California Governor

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letters

MORE ON KOLKO'S COMPLAINT

I was most interested in your listing of faculty members [*REASON FACULTY REGISTRY,* January], and especially the response of Gabriel Kolko [objecting to his proposed inclusion in the Registry]. I think that Kolko is incredibly misinformed as to the nature and place of the contemporary libertarian movement. He just doesn't seem to realize that the "persistent use" of his works does not (and indeed can not) "buttress American *conservative* ideology." He simply *assumes* that libertarians are conservatives, and that they are way off base. The truth is, of course, that *Kolko* is off base. The value of his writings (such as *THE TRIUMPH OF CONSERVATISM, RAILROADS AND REGULATIONS,* and *THE POLITICS OF WAR*) lie in the fact that they constitute valid empirical refutations of *statism*—but all kinds of statism —state socialism just as assuredly as state "capitalism." The fact that Kolko has "been a socialist and against capitalism all of my life" is simply a personal quirk and contradiction, since his works in no way validate the socialistic position, but on the contrary, do a great deal in suggesting the need for a *truly* free market as the basis of a politically free and peaceful (nonimperialistic) society.

William Danks
Dept. of Political Science
University of Hawaii
Honolulu, HI

SYMMS A CONSERVATIVE?

I believe you have done the Libertarian political movement a disservice in the February issue of *REASON.* The implication of the cover of that issue is that the featured interview with Congressman Steve Symms will provide an insight into libertarian politics.

Symms is a conservative, not a libertarian. He brings to Congress an inconsistent conglomeration of views, many of which are good but some of which contain the seeds of statism as do the views of all of his colleagues.

To defend his statist position on amnesty Symms cites the incredible reason of "a well disciplined family, football in college and three years in the Marine Corps." If the Libertarian Party is to succeed in convincing those members of the movement who are opposed to political action that such action can be efficacious in the right for liberty, we must disassociate ourselves with the political philosophy of men like Congressman Symms.

Edward H. Crane
Vice Chairman, Libertarian Party of California
Los Angeles, CA

HE'S VALUABLE, BUT . . .

I am appalled. Rep. Symms is a valuable man to have in Congress but he is not a libertarian. Libertarians are neither equivocal on drugs, nor have "corpuscular" reactions to the amnesty issue.

It's bad enough having 99% of the press making no distinction between libertarians and conservatives, but when *REASON* starts doing it . . . .

R. E. Cleary
Arlington, MA

By presenting a full-length interview with Congressman Steve Symms, REASON *desired to provide our readers an opportunity to judge for themselves as to Symms' credentials as a libertarian. Although Symms' candidacy was endorsed by the Libertarian Party,* REASON *emphatically does not endorse all of his positions. While he has been "on target" on many issues, on the whole, Symms' record is—as we have previously noted—"somewhat disappointing." For those that wish to learn more about the views of the first Congressman elected with the endorsement of the LP, a limited supply of copies of the February issue is still available at the price of $1.00 each.—Ed.*

NONCOERCIVE SEX EDUCATION

Ralph Raico's "Against Sex Education" [February] could just as well have been entitled "Against driver education" or "Against American history classes", since its arguments (as distinct from its expressions of visceral feeling) have no specific connection with sex. Raico does not show that the theft of money from taxpayers is any more reprehensible when it goes to support sex education than when it goes to support volleyball instruction, nor that the "imposition upon a captive audience of a process designed either to change or to reinforce certain . . . values" is more severe or more objectionable in the case of "sexual values" than in the case of economic or political values. The details of how pregnancy comes about, how various contraceptives work and how effective they are, and how venereal diseases are transmitted, detected, and treated are as amenable to classroom presentation as is physics or Latin, and Raico has shown no respect in which classes covering such matters would be objectionable in voluntarily supported noncompulsory schools. Certainly attendance at such classes is unlikely to inhibit students from following Raico's recommendation that they learn about sex "at parties, in bars, in johns, . . . and 'the gutter' " as well as from books. But while I share Raico's respect for the educational value of "the gutter" and of bars (though we differ about johns), I would remind him that the gutter is not a place where one is likely to acquire the factual information about pregnancy and disease that one needs as a basis for responsible action.

James D. McCawley
Dept. of Linguistics
University of Chicago
Chicago, IL

QUESTIONS FOR HOLT

I wish Boston newspapers were as lenient with letter-writers as is *REASON;* a letter as offensive as John Holt's (*REASON,* Feb. '74) would doubtless never be published by the Boston Globe or the now-defunct Hearst paper.

Let's begin with Holt's attack on a book called *THE DISASTER LOBBY,* a book which, presumably, he has never read, since his criticism aims at the book's ad and the fact that it was placed in a libertarian publication. His proofless premise here is that avaricious and greedy corporation executives expect to dupe dummy libertarians by presenting facts about Disaster Lobby propagandists and the eensy little realities which they are guilty of either overlooking or covering-up. Uh, speaking of cover-ups . . . Holt can't stand the idea that someone might prove some businessmen not guilty of . . . virtually anything. *Which* individuals, John Holt, are guilty of violating rights of other individuals; what are their names and addresses and occupations and how might we lay hands upon them? Until you can answer me, it is impossible to take you seriously.

And it makes me want to puke when Holt states that we should not question the *existence* of government and power; in a normative tone, he would aim at a more "just" (egalitarian) distribution of force and power. Would he wish to receive his fair share of a broken nose, or a portion of the time which I have spent in a Navy brig? Spreading evil around will not eliminate it, but rather pollute those as yet unsullied by it. . . .

Steve Andrews
Marblehead, MA

ANSWER FOR HOLT

With regard to John Holt's letter in the February issue of *REASON, GRAVY PLANET* was published in paperback under the name of *THE SPACE MERCHANTS,* not *THE PLANET MERCHANTS.* More importantly it was not written by Poul Anderson but by C. M. Kornbluth (with Frederik Pohl). I suggest that Mr. Holt check his sources a little more carefully. Also if Mr. Holt knows of a method for manufacturing automobiles in a garden, I'm sure everyone would be delighted to hear it.

As for Holt's "little question" [concerning the "Mafia problem"] in the March issue of *REASON,* if he would bother to read a book on libertarianism he might find it answered. *THE MARKET FOR LIBERTY,* for instance, has an entire chapter devoted to the question of organized crime.

Epicurus was an ancient Greek philosopher, not an ancient Roman one as is stated in [John Hospers' article] "The New Epicureans" [March].

Jack C. Kurtz
Charleston, SC

UNDERSTANDING LIBERTARIANISM

I am writing this letter in response to the letter from John Holt ["Taking Government Seriously"] in the February issue of *REASON.* I believe he has some misunderstandings about libertarianism, which I hope I may be able to correct to his satisfaction.

First of all, I must agree with him that the question of power and protection from it has not been adequately explored in the libertarian literature. There have been many attempts to describe libertarian alternatives of protection and justice, but these are always open to skepticism because it is so difficult to postulate what form a radically different society might take.

Even if the form is obscure, the principles are not. Libertarians are attempting to build a totally consistent philosophy based on the facts of human existence, which include a recognition that individuals very often do violence to others. This very observation makes it so necessary that government be done away with, since government claims for itself that which no violent individual or group could ever have: legitimacy.

Of course there will always be individual and gang violence, and some sort of institutions will have to be formed to deal with it. I am not trying to deny the difficulties of this. But I do believe that at least when people come to realize that some people have no right to rule other people, the situation will have improved a great deal.

A more serious charge is that libertarians are "rather innocent apologists for rich

QUALITY IN MEDICINE VS POLITICAL QUACKERY: YOU CHOOSE

You've heard of Uncle Sam the Medicine Man. It is time for you to meet Citizens for Quality in Medicine. Formed by Alaska libertarians, this Social Action group is on the heels of its first victory, and it is political medicine that is on the run. In REASON you read about the Professional Standards Review Organizations law. Now read about CQM's attack on bureaucratic medicine.

PSRO sets up local panels to see that:
1 Doctor-patient records are an open book to HEW chief. Remember Daniel Ellsberg!!
2 Doctors' treatments meet government-set, national averages, not your doctor's judgment.
3 Patient hospitalization is decided by PSRO cost control.
4 Patient's choice of doctor is controlled by PSRO board.

CQM'S Action
1 Provided Congressmen evidence of consumer support to repeal PSRO.
2 Mailed information to doctors of Alaska urging their aid of the Assoc. of American Physicians and Surgeon's legal suit against HEW chief and PSRO.
3 Began strategy with John Zeigler of SPEAK OUT! to raise money for a professional lobbying campaign.
4 Began plans with a libertarian lobbyist.

We are loud and prone to action. It is the rights of the buyers of medical services we are defending. All social and statistical evidence indicates that low cost, personal care, and customer choice are available through free market medicine. And with the Nixon-Kennedy National Health Insurance passed and involuntary sterilization laws before 16 State legislatures, the need to spread this evidence is urgent. We may well be on the eve of a Police State in the medic uniforms of obedient civil servants.

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Citizens for Quality in Medicine—Box 2724, Kodiak, AK 99615. Director: Paul Beaird, editor of Alaska LP ACTION, computer programer.
Advisory Board: Dr. Robert Jaggard, MD, recent President of AAPS, speaker at recent Illinois LP convention.
Campaign Advisor: John Zeigler and SPEAK OUT! staff.
Intellectual Ammunition: **Hazardous To Your Health** by Marvin Edwards.

A C T I O N N O W !

Yes . . . Hell, Yes, I am ready for social action that can succeed, and I oppose Big Brother playing doctor with human lives. I am enclosing the following donation:

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LIBERTARIAN ACTIVISM IS EFFECTIVE

and powerful people who do not believe in freedom at all—except for themselves and their friends." I suspect that this impression is caused mainly by the background of many libertarians. Many of us were originally conservatives, and there is still a lot of conservative philosophy masquerading as libertarian. In general, libertarians side with conservative economics, because it more closely adheres to the facts of life than liberal economics. However, conservatives believe that business has been the innocent partner in the business-government-consumer triangle. Numerous cases have been documented which instead show that business has often actively agitated for special regulations, to enhance its position at the expense of others.

Libertarians do not condone allowing corporations "to do whatever they want, at whatever the cost to the earth and the living creatures on it." We are in no way opposed to ecology and conservation, when it is supported by scientific fact instead of emotion. A true libertarian makes apologies for no one, because he realizes that business, government, and the general public have all contributed to the loss of freedom. Instead he tries to select for criticism those people and institutions which have been the worst offenders. In doing so, a libertarian must always use his conception of an ideal society for comparison, rather than defending the status quo as conservatives do.

This is where many of the bad impressions arise. Since it is such a difficult task, many libertarians have not been able to separate what we have now from what could be. Thus, some of our philosophy sounds grossly unfair when viewed in the light of today's society.

For example, the proper economic solution to the present energy crisis is to allow prices and profits to rise, in order to stimulate production. This is the most practical solution, and in a libertarian society it would also be moral. However, we do not now live in a libertarian society. The very companies who would benefit from such action have already received many special favors, and are part of the large state capitalist establishment. Thus, we are faced with the dilemma of not knowing whom to support, because the bad guys are on both sides. I have seen numerous articles on how to correct injustices done by governments, but not one article yet on what to do about past injustices caused by business and other "private" institutions.

Unless we wish to be totally stalemated, it is necessary to take stands on issues. However, whenever we choose the lesser of two evils in a situation, we must make it very clear that the choice was pragmatic, and does not constitute complete philosophic agreement. In fact, there is very little in contemporary society that a libertarian can wholeheartedly support. We are really in search of two things that the world has a real shortage of: freedom and justice for all.

Paul Bilzi
State College, PA

HOLT ON "SOCIAL CONTRACT"

I strongly commend to you and your readers Richard Goodwin's three part article on The American Condition, which begins in the Jan. 21, 1974 issue of *THE NEW YORKER.*

Mr. Goodwin makes a most important point, that does not always seem well understood by contributors to *REASON,* that individual liberty in any human society or community must be based on an ethical or moral vision, an awareness of and respect for common interests, concerns, and needs, an understanding that the part of space-time which I call Myself includes many parts of the lives of many other people.

"Every man for himself, and the devil take the hindmost"; "Do whatever you can get away with"; "I've got mine, screw you Jack!"; "Winning isn't everything; it's the only thing"—such attitudes are recipes, not for liberty, but for tyranny.

Or, to put it a little differently, the statement, which is quoted with enthusiasm by at least a few self-styled libertarians, that because I have not signed the "social contract" it does not exist and I am not bound by it, is a most ignorant, shallow, short-sighted and self-defeating remark.

May I also recommend to your readers a most vivid and exciting piece of fiction, *THE FRIENDS OF EDDIE COYLE,* by George Higgins. It is a very plainly and honestly told story about people for whom violent crime is a way of life—and I ask once again, as I did earlier about the Mafia, if we did away with government, what would we do about such people?

I hope you may find it possible to print this letter. It goes without saying that if I did not think that you and your readers had a certain political and philosophical importance in these difficult times, I would not have bothered to write it.

John Holt
Boston, MA

John Holt is the author of a number of books on education, including HOW CHILDREN FAIL *and* HOW CHILDREN LEARN.*—Ed.*

Reason's Letter of the Month

The letter below, by subscriber Richard Grant, appeared in the *LOS ANGELES TIMES* of February 12, 1974.

Cohen's excellent article on business and politics perhaps overlooked the underlying reason that businessmen seem reluctant to seek political office. The two activities are based on opposing premises: commerce depends on voluntary exchange, while political action is based ultimately on force.

The successful businessman (at least, the one who doesn't survive on political favors such as tariffs, subsidies, government contracts, etc.) must depend on persuasion, cooperation and productive skill. The politician, on the other hand, whose programs are enforced ultimately by the tax collector and the jail cell, deals in a different coin entirely.

Philosopher Will Durant observed that "civilization begins with the first voluntary act—and ends with the last." And government, let us not forget, is not a voluntary institution. Reliance on political action does not represent "progress," but a slow retreat to barbarism.

"Good people" should not get into politics; they should get out of politics. Their presence in the political arena merely lends respectability to a process which, by its coercive nature, is inherently destructive. The solution to our problems does not lie in political action at all, no matter how well intentioned, but in the private, voluntary alternatives of a free society.

R. W. GRANT
Manhattan Beach

REASON subscribers are encouraged to write letters to the editor of their favorite newspaper, magazine, or journal, presenting libertarian views on topics of current interest. Each month *REASON* selects the best such published letter for republication in this space, and honors the writer by a six-month extension of his or her *REASON* subscription. Send copies of *your* published letters to Reason Letter of the Month, Box 6151, Santa Barbara, CA 93111.

AVOIDING SOCIAL SECURITY

I would like to call the attention of your readers to a provision of the Internal Revenue Code which can exempt certain persons from paying the 5.85% or 8% Social Security tax.

Under Internal Revenue Code Section 1402(e), persons who belong to religious orders which are opposed to public insurance can file form 4361 with the Internal Revenue Service and be exempt from paying the 8% self-employment tax.

Lloyd Taylor
San Francisco, CA

See this month's "Trends" for further information on tax avoidance.—Ed.

COURAGE TO BE HAPPY

It is ironic that Harry Browne, who seems to care very little for missionary work, will have such a widespread effect among the general public through his recent publication, *HOW I FOUND FREEDOM IN AN UNFREE WORLD.* Yet even besides his book's entertainment value, and in light of the lucid and quite accurate critique by Dr. John Hospers (*REASON,* March 1974), Browne offers serious thoughts which should not be ignored by many self-assured libertarians among his readers.

Browne does acknowledge that a person may want to change his personality, but as he writes (p. 312): "Understand, however, that the change will probably be a long-term project. Don't let it interfere with what *does* make you happy." Merely recognizing the wisdom of a particular moral theory does not mean that the person will automatically be basking in golden rational bliss by trying to put the moral principles into practice. The incorporation of conceptually accepted beliefs into one's emotional superstructure in a long and often painful process which may end in failure. It is a sad waste of irretrievable time not to do those things which one enjoys here and now while still working towards an improved character. Should one instead try to repress all "illogical" and "contradictory" emotions and claim to have become the new Libertarian Man (or Woman) overnight? (Readers of Branden know what havoc such repression can produce in a soul.)

I concede that it is possible for a libertarian to enjoy political activism in and of itself, but I wonder how many people working in the movement are there because they have nowhere else to go? If that happy day ever arrives when we can leap out of bed in the morning and cry, "Hot dog! It's great to live in a free world!" what will the activists do then? This is no facetious question: as Harry Browne argues, especially in Part II, there are great numbers of ways that most of us can achieve what we want in the present irregardless of the diverse "traps" which surround us. I wonder how many libertarians feign a rationality that isn't real for them out of fear of real independent judgment? How many go to meetings and rallies when they deeply would rather watch an old, friendly movie? How many buy the "right" books (and never read them) or contribute to causes and campaigns when there is a more personal investment which would be more satisfying?

In short, how many libertarians have the courage to be happy?

Glenn E. Sieferman
Socorro, NM

Letters from readers are welcome. Each receives editorial consideration, although only a selection can be published and none individually acknowledged. They should be kept as brief as possible and are subject to condensation. Letters submitted for publication in this column should be typed, double-spaced. Send letters to REASON, P.O. Box 6151, Santa Barbara, CA 93111.

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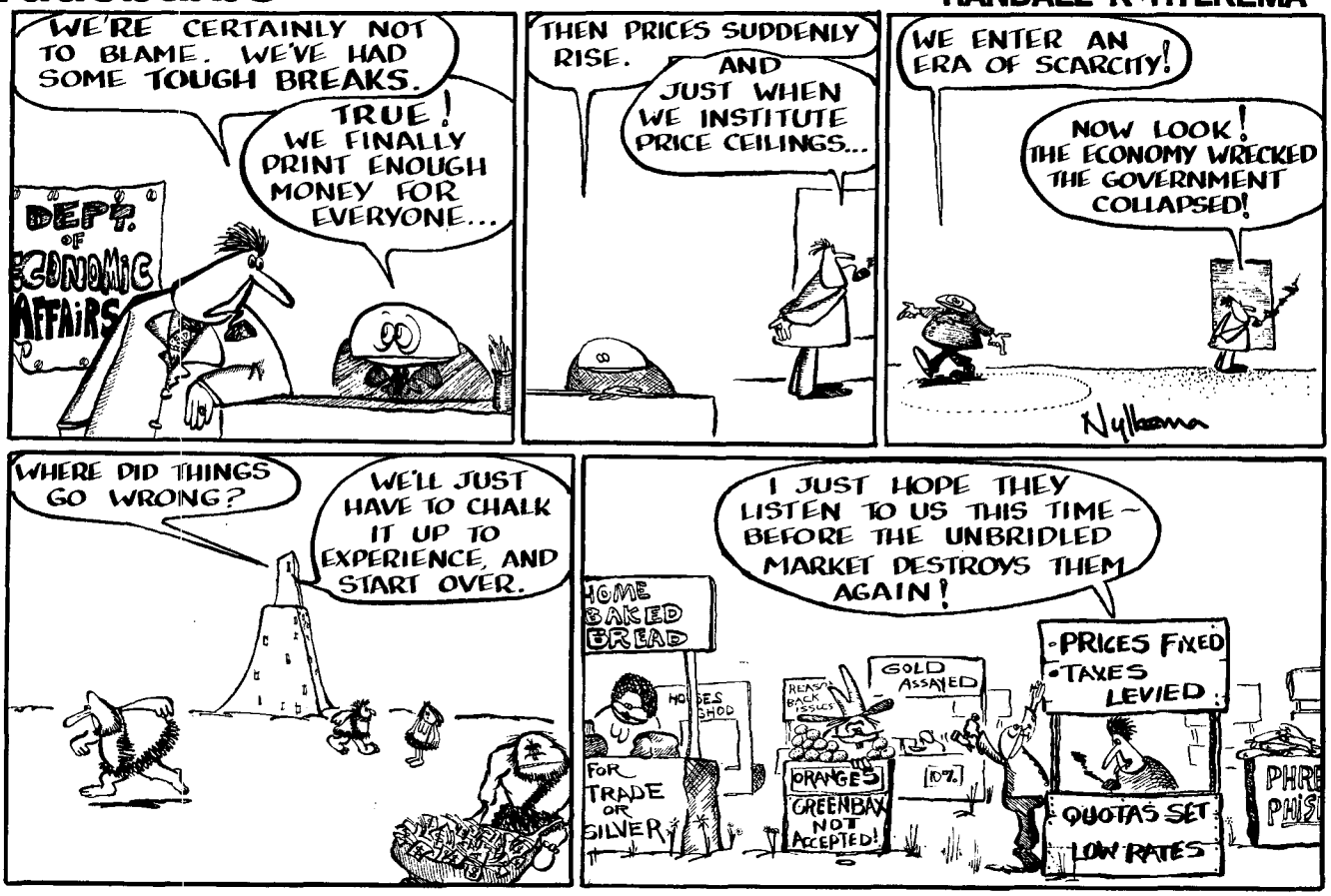
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PERSONAL

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ALASKA LIBERTARIAN, male, 30, fisherman, homosexual, who loves the wilderness, early music, field biology, poetry, and most any sort of new knowledge, seeks contact with others interested in open personal development. Reply to Box AH, *REASON.*

OPERATION TRANSITION was meant to fail. I am searching for reasons why. I would appreciate comment from those having knowledge of this project and associated injustices. Write: *Dan Bennett,* 34 Pine Tree Loop, North Little Rock, AR 72116.

I AM DESIGNING A RURAL RETREAT to be built in the hills of central Kentucky and am looking for 16 to 20 people to join me in this project. The basic structure would be mutually owned with common living areas downstairs and private sleeping rooms upstairs. Contact: Harry L. Moyer, 2806 Rockford #D-7, Louisville, KY 40216.

TO THE MAN WHO WORSHIPS THE UNKNOWN GOD IN HIMSELF—who stands pride's mountains above the insignificant others and molds his world from values unperceived by them: The strength, openness, uncompromising courage and serene joy you have always sought do indeed exist, and await your reply. *Marjorie Levin,* 3572 Central, Fort Myers, FL 33901.

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MAY 27, 1974
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PHILADELPHIA AREA: I am trying to arrange the playing of one of *Dr. Leonard Peikoff's* philosophy courses. Anyone interested contact Arnold Baise, (215) 742-7478 (evenings).

I WOULD LIKE TO CORRESPOND WITH OTHER GAY MEN, especially in the Chicago-Milwaukee area who are students of Objectivism or libertarians. Write: *Bill McE.,* Box 1003, Chicago, IL 60690.

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